INCOME TAX REPORTS

A JOURNAL OF THE LAW OF INCOME TAX

WITH REPORTS OF

INDIAN AND SELECT ENGLISH CASES

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VOLUME IV.

1936.

THE COMPANY LAW INSTITUTE OF INDIA,

THYAGARAYANAGAR,

MADRAS.

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Mode of Citation.

1936 I.T.R.

1936 I.T.R. Eng. Cas.

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THE

INCOME TAX REPORTS

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PROGRESS OF THE LAW OF INCOME TAX IN 1935.

To begin with AGRICULTURAL INCOME, there have been some doubts as to whether, when a money-lender in the course of his business advances money on mortgage and appropriates the income of the mortgaged property in lieu of interest such income is exempt as agricultural income. A Special Bench of the Madras High Court held in *Commissioner of Income Tax, Madras* v. *Janab Haji Muhammad Sadak Koyee Sahib* (1935 I.T.R. 4) that such income is agricultural income even though it is credited towards interest. This question has now been settled beyond all doubt by the Privy Council in the recent case of *Commissioner of Income Tax, Bihar and Orissa* v. *Sir Kameshwar Singh* [1935 I. T. R. 305] in which their Lordships have laid down in clear terms that the scheme of the Indian Income Tax Act is to exclude agricultural income from the scope of the Act 'however or by whomsoever received, and that, if in the course of a money-lending business a loan is advanced on mortgage of immovable property and the money lender pays himself the principal and interest of the loan by appropriating the income of the mortgaged properties, such income is agricultural income and cannot be assessed to income tax as interest received in the course of a money-lending business. Agricultural income, their Lordships have observed, does not lose the benefit of the statutory exemption of agricultural income and become assessable as business profits merely because it was received by the assessee not as an ordinary proprietor or landlord but as part of the income, profits and gains of a money-lending business.

The question whether excess income received by a managing co-owner in consideration of his services as manager over and above his share as a co-owner is assessable as salary or exempt as agricultural income was considered by the Lahore High Court in *Major Conville* v. *Commissioner of Income Tax, Punjab* (1935

I.T.R. 404). In the opinion of the Lahore High Court such excess income is assessable as salary. The distinction between agricultural income and annuities received as consideration for sale of immovable property is pointed out by the Privy Council in *Maharaj Kumar Gopal Saran Narain Singh's Case* (1935 I. T. R. 237). In this case a person sold his property stipulating in return for certain annual payments for a number of years and the Privy Council held that the annual payments received by the vendor cannot be treated as agricultural income as it was not rent or revenue derived from land but money payable under a contract imposing a personal liability on the purchaser.

As to ANNUITIES, in *Gopal Saran Narain Singh* v. *Commissioner of Income Tax, Bihar and Orissa* (cited above), the Privy Council has held that when the owner of an estate sells the estate in consideration of receiving an annuity for his life, the annual payments received by him are 'income' in his hands and not receipt of capital in instalments. This decision further establishes that for income to be taxable it need not necessarily be a profit or gain to the assessee. Anything which can properly be regarded as 'income' is taxable even though it is not a gain or profit to the assessee.

Regarding APPEALS TO PRIVY COUNCIL, in the case of *Maharajkumar of Visianagaram* (1935 I. T. R. 155) the Allahabad High Court has re-iterated the view that no appeal lies to the Privy Council from a judgment delivered on a reference under Section 66 unless the case is certified by the High Court as a fit one for appeal; and the Calcutta High Court has held in *The Hungerford Investment Trust case* (1935 I. T. R. 188) that the jurisdiction conferred on the High Courts by Section 66 is neither original nor appellate jurisdiction but a special jurisdiction and that the procedure to be followed in the matter of appeals to the Privy Council is therefore governed by the provisions of the Civil Procedure Code and not by the Rules contained in Chapter XXXIII of the Calcutta High Court Rules relating to Original Side matters.

The expression "ASSOCIATION OF INDIVIDUALS" in Section 3 of the Act has been held in *In re Elias and others* (1935 I. T. R. 408) to include co-owners who purchase and enjoy property jointly, even though they hold definite shares in it. The case, as we have stated, is of doubtful authority.

Coming to BAD DEBTS, the Lahore High Court has held in *Hukum Chand Jagadharmal* v. *Commissioner of Income Tax*,

Punjab (1935 I.T.R. 211) that though whether a debt is bad and when it became bad are questions of fact to be decided by income tax authorities, yet their conclusions must be based on relevant and admissible evidence and the question whether there is such evidence to support the conclusions arrived at by the income-tax authorities is a question of law open to consideration by the High Court.

On Best Judgment Assessment there have not been many rulings but the decision of the Calcutta High Court in *Keshardeo Chamria, In re* (1935 I.T.R. 418) has to be noted. The Calcutta High Court has held in this case that the only questions that can be raised in an appeal against an order under Section 27 and in the case of an assessment under Section 23 (4) of the Indian Income Tax Act are (1) whether the assessee was prevented by sufficient cause from making the return required by Section 22; or (2) whether he received a notice issued under Section 22 (4) or Section 23 (2); or (3) whether he had a reasonable opportunity to comply with the terms of the notices; or (4) whether he was prevented by sufficient cause from complying with the terms of the notices, and that, all these being questions of fact, there can be no reference under Section 66 (2) or (3) of the Income Tax Act from an order under Section 23 (4) or an appellate order under Section 27.

There are some important cases on Business Expenditure. In the *Imperial Chemical Industries (India) Ltd., In re* (1935 I.T.R. 21) it was held that moneys paid to an agent on termination of his agency as compensation for loss of the agency, and in consideration of the agent agreeing to assist the assessee's employees in getting an insight into the working of the business and for not entering into competition with the assessee for some years was business expenditure. The expenditure was not of a capital nature but an expenditure falling within Section 10 (2) (ix) inasmuch as the assessees were not nurturing or protecting a new business or purchasing anything in the nature of goodwill but only securing advantages for their undertaking and facilities for future operations and inasmuch as the payment was made out of the circulating capital and did not result in any new asset or addition to the fixed capital of the assessees. The judgment contains a learned discussion of the considerations which ought to be borne in mind in deciding whether an item of expenditure is business expenditure or capital expenditure.

The principle laid down by the Privy Council in the *Pondicherry Ry. Co.'s Case* that payments made by an assessee

from his income to third parties under agreement to pay them a share of the profits are not allowable as business expenditure, was applied by the Bombay High Court in three cases: *Commission of Income Tax, Bombay* v. *C. Macdonald and Co.* (1935 I.T.R. 459), *Tata Hydro-Electric Agencies Ltd.* v. *Commissioner of Income Tax, Bombay* (8 I.T.C. 228) and *Indian Radio and Cable Communications Ltd.* v. *Commissioner of Income Tax, Bombay* (8 I.T.C. 223). In *Hiranand Jayaram Singh's case* (1935 I.T.R. 309) in which a salt contractor who had deposited certain Government securities with the Commissioner of Salt had to sell these securities at a loss, as the system of deferred payment on security was stopped by the Government, it was held that the loss was a capital loss and not business expenditure incurred in the salt business. In another case, litigation expenses incurred by a company which had taken a lease for quarrying slate, to defend their right to quarry against persons who challenged their right was held to be in the nature of capital expenditure [*Kangra Valley Slate Company* v. *Commissioner of Income Tax*, (1935 I.T.R. 324)] and the question whether expenditure incurred with a view to resume a business which has ceased to work is allowable as business expenditure against profits from the assessee's other business was answered in the affirmative by the Madras High Court in *The General Corporation Ltd.* v. *Commissioner of Income Tax, Madras* (1935 I.T.R. 350). Before leaving this topic we wish also to invite the attention of our readers to the decision of the House of Lords in *Van Den Bergh's Case* (1935 I.T.R., English Cases, page 17) which contains a clear exposition of the principles governing the determination of the question whether an item of receipt or expenditure relates to capital or revenue.

With regard to the assessment of COMPANIES we may first refer to the case of *The Calcutta Stock Exchange Association Ltd.* (1935 I.T.R. 105) in which the Calcutta High Court held that the proviso to Section 9 (2) of the Income Tax Act which lays down that 'where property is in the occupation of the owner for the purposes of his own residence' the annual value of such property shall be deemed not to exceed 10 per cent. of the total income of the owner does not apply to property occupied by limited companies for their own purposes. In their Lordships' view this provision is intended only to apply to human beings and not fictional persons like limited liability companies. In *Harvey* v.

Commissioner of Income Tax, Madras, it has held that, though in order to assess the shareholders of a company on the profits of the company which have been reasonably allowed to accumulate without being distributed as dividends it is necessary under the Indian Income Tax Act to show that the profits were accumulated with the intention to evade income tax, yet intention is a matter which need not directly be proved but may be inferred from the circumstances. In this case a company formed in 1926 did not distribute any of its profits till 1930 though it had very large profits and the directors were not able to give any explanation and the High Court held that the income-tax authorities were entitled to come to the conclusion that there was an intention to prevent the imposition of tax and to assess the shareholders under Section 23-A. The principle laid down by the House of Lords in *Blott's case* and followed in *Fisher's case* that where a company capitalises its accumulated profits and distributes them as debentures to the shareholders there is no distribution of profits and the shareholders cannot be assessed to income tax in respect of the value of the debentures was applied by the Calcutta High Court in *Sir David Yule's Case* (1935 I.T.R. 163). The principle was applied even though it was clear that this device was adopted in order to evade income-tax. In an Oudh case, *Income Tax Officer, Lucknow* v. *Lucknow Sugar Works*, it has been held that where a company upon which an assessment has been made is wound up before payment of tax, the Income Tax Officer has, like other creditors of the company, to go before the Official Liquidator and prove his debt and that it is open to the latter to reject the claim if he thinks the assessment is not justifiable. We have expressed our doubts regarding this decision already.

The Hungerford Investment Trust Ltd., In re (1935 I.T.R. 65) decides a question of considerable importance relating to the exemption of dividends paid to shareholders of limited companies. This case establishes that sums received by way of dividends as shareholder in a company are exempt from tax under Section 14 (2) (a) of the Indian Income Tax Act where the profits or gains of the company have been assessed to income-tax *even though those dividends were in fact to some extent paid out of profits or gains in the hands of the paying company which were free from taxation altogether*. This interpretation of the section, it may be noted, enables individuals or companies to escape payment of income-tax

altogether in certain cases though the object of Section 14 (2) (a) was only to avoid double taxation.

There are two important pronouncements relating to the assessment of CO-OWNERS. In *In re Elias and others* decided by the Calcutta High Court (1935 I.T.R. 408) four persons purchased a building in definite shares and enjoyed it as tenants in common empowering one of them to manage the property on behalf of all. The High Court held that these four persons could be assessed to income-tax and super-tax on the income derived from the building as an 'association of individuals'. This decision, as we have stated in our Notes and Comments, seems to overlook the distinction between property owned by an association and property owned by the members individually in distinct shares though enjoyed in common and does not appear to be sound. The other decision, *Major Conville* v. *Commissioner of Income Tax, Punjab* (1935 I.T.R. 404) deals with the question whether income received by the managing co-owner of a joint estate in consideration of his services as manager *over and above his share as co-owner* is exempt from tax as agricultural income or assessable as salary. The Lahore High Court has held in this case that in such cases the income received by the managing co-owner in excess of the share to which he is entitled by virtue of his right as co-owners that is, the income which he takes in return for his services, is assessable as salary and is not agricultural income.

The conflict which prevailed in India as to whether in calculating DEPRECIATION OF MACHINERY where such machinery has been transferred 'the original cost to the assessee' should be calculated with reference to the original cost of the machinery to the purchaser or to such cost to the original owner has been set at rest by the Privy Council in *The Income Tax Commissioner, Madras* v. *The Buckingham and Carnatic Company Ltd.* (1935 I.T.R. 384). The Privy Council has held that such cost should be calculated with reference to the cost to the actual assessee, that is, the purchaser. The opinion expressed by the Madras High Court in *Massey's case* (56 M.L.J. 431; 3 I.T.C. 302) stands overruled and the view of the Bombay High Court in *Saraspur Mills Co. Ltd., In re* (56 Bom. 129) is approved. Another decision with regard to depreciation to which reference may be made is *Sadhucharan Roy Choudhury and others, In re* (1935 I.T.R. 114). Where a factory is leased out the lessor is entitled under this ruling to claim depreciation allowance in respect of the buildings and machinery of

the factory. The contention of the revenue authorities that leasing out a factory is not a business and that the buildings and machinery leased out cannot be held to be used for the purpose of the business of the lessor within the meaning of Section 10 (2) (vi) was overruled in this case.

(To be continued)

Assessment of Indian Branches of Foreign Insurance Companies.

In *the National Mutual Life Association of Australasia* v. *The Commissioner of Income Tax, Bombay*, to be reported, the Judicial Committee have reversed the decision of the Bombay High Court reported in 1933 I.T.R. 357 and laid down some important rules relating to the assessment of the Indian branches of non-Indian insurance companies. The main statutory provision relating to the assessment of such branches is, it will be remembered, Rule 35 of the Income Tax Rules which provides that in the absence of more reliable *data* the total income of the Indian branches of Non-Resident insurance companies may be deemed to be the proportion of the total income, profits or gains of the companies corresponding to the proportion which their Indian premium income bears to their total premium income. The Judicial Committee have discussed in this case the comparative value of the balance sheet and valuation reports and explained the conditions under which Income Tax Officers may resort to the method prescribed in Rule 35. An insurance company had with their return produced the revenue account and balance-sheet of their Indian business and had also supplemented it by a valuation report of a prior period and contended that these were more reliable data than the method prescribed in Rule 35 and that the income tax authorities could not therefore assess them under Rule 35. The Privy Council held that in the case of life assurance companies the most reliable data to arrive at the profits are the periodical valuation reports and held further that a single valuation report as at the end of the year of account would not be sufficient and that consequently in the instant case the Income Tax Officer was right in holding that the information submitted did not afford more reliable data than the method prescribed by Rule 35. Their Lordships point out that the amount of interest earned on investments, though it is an element in the ascertainment of the income, profits or gains, is not by itself a

reliable datum for such ascertainment. The result of the decision is that Income Tax Officers would be justified in applying the method prescribed by Rule 35 if companies do not produce their periodical valuation reports.

Assessment of Mutual Insurance Companies.

The next point decided in this case deals with the method of applying Rule 35 in the case of mutual insurance companies. The Bombay High Court was of opinion that premiums received from participating policies, although no profits or gains, were nevertheless premium income, and that the premiums from participating policies could not therefore be excuded in computing the premium income for the purposes of applying Rule 35, but the Judicial Committee have held that even assuming that the expression ' premium income ' in Rule 35 would include premiums received in respect of participating policies, ' the total income, gains or profits of the companies ' referred to in that rule is the income, profits or gains as they would be ascertained for the purposes of the Act and that in calculating such income for the purposes of Rule 35 the premiums received from participating policies should be excluded.

Failure to Make Return in Prescribed Form : Whether justifies Best Judgment Assessment.

Where a return is made which is not in the prescribed form, can the income tax authorities regard it as no return and make a best judgment assessment under Section 23 (4)? Their Lordships have expressed their opinion in the above mentioned case on this short but important question. The Commissioner of Bombay held in this case that as the company did not make a return in the prescribed form a best judgment assessment could be made, and the Chief Justice of Bombay also said in his judgment that failure to make a return in the prescribed form justified the Commissioner in making an assessment under Section 23 (4). The Judicial Committee said that though this point did not directly concern the questions of law referred, their Lordships felt some doubt as to the Commissioner's view that the company had failed to make a return within the meaning of Section 22 (4), thereby expressing their disapproval of the opinion of the income tax authorities and the Bombay High Court.

PRIVATE ENQUIRIES BY INCOME TAX OFFICERS

Can an Income Tax Officer or an Assistant Commissioner make private enquiries and take into consideration the result of such enquiries in making an assessment? This very important question was raised we presume for the first time before the courts. In a recent case before the Allahabad High Court *Gopinath Naik* v. *Commissioner of Income-tax, U. P.* (1936 I.T.R. 1) NIAMATULLAH, J., and BAJPAI, J., before whom the case came on for hearing differed. The case was therefore referred to a third judge, SIR SHAH SULAIMAN, C. J. The opinion of the Chief Justice which ultimately prevailed is as follows :—

SULAIMAN, C. J.'s VIEW

(1) When a return is received by an Income Tax Officer he is not bound to accept it as correct and complete. He can make enquiries as to whether there is reason to suspect that the return is incorrect or incomplete. These are administrative acts and no objection can be taken to such private enquiries even if they are carried on behind the back of the assessee.

(2) But if the Income Tax Officer is of opinion that the return is incorrect and incomplete and proceeds to serve a notice under sub-Section 23 (2), the proceedings assume the character of a 'judicial enquiry' and the Income Tax Officer can take only such 'evidence' as the assessee may produce and such 'evidence' as that Income Tax Officer may require in rebuttal of the evidence produced by the assessee. Such evidence should be taken in the presence of the assessee and the Income Tax Officer cannot make any private enquiries after the issue of notice under Section 23 (2).

(3) He may, however, take into consideration the previous years' assessments, even best judgment assessments.

(4) If an assessment is based partly on the result of private enquiries and partly on evidence which is legally admissible, *e. g.*, prior years' assessments, the finding is improper and vitiated so far as it is based on private enquiries; but if the finding could be supported on the other admissible evidence in the case without taking into account the result of the private enquiries, then the finding would not be illegal according to the principle underlying Section 167 of the Indian Evidence Act.

BAJPAI, J.'s VIEW.

This opinion agrees in many respects, though not in all, with that of NIAMATULLAH, J, but BAJPAI, J. has clearly dissented. In

his view an Income Tax Officer is not a judicial officer and the proceedings before him are not judicial proceedings. The rules of the Evidence Act are not applicable to proceedings before such Officers. They are revenue officers and are, as such, from the nature of things, bound and entitled to make private enquiries. But before making an assessment on the basis of such enquiries they are bound, in consonance with principles of natural justice, to give an opportunity to the assessee to rebut or explain the circumstances gathered by them in their private enquiries.

OUR COMMENTS

Though the weight of judicial authority is in favour of the former view, that is, the view of SULAIMAN, C. J., we prefer the view of BAJPAI, J. In our opinion (i) for a judicial proceeding there must be two parties. The Crown will surely go unrepresented and the proceedings will be entirely one-sided if there is nobody to collect evidence regarding matters which appear suspicious in the assessee's accounts ; (ii) if, as SULAIMAN, C. J., concedes, Income Tax Officers can make private enquiries after a return is received and before they issue a notice they will be unfit to conduct further proceedings as 'judicial proceedings' ; (iii) Section 37 clearly implies that proceedings before Income Tax Officers are not judicial proceedings except for the purposes of Sections 193 and 228 and 196 of the Indian Penal Code ; (iv) the definition of 'Court' in the Evidence Act does not include Income Tax Officers and (v) as there is no provision making it obligatory on Income Tax Officers to record the evidence of witnesses in the exact words of the witnesses as in Civil and Criminal Courts it would be impossible to sever the admissible from the inadmissible portions of the evidence relied on by them and to apply Section 167 of the Indian Evidence Act.

If the view which has prevailed with the Allahabad High Court is right, it is very essential that all the Income Tax Officers should thoroughly study provisions of the Indian Evidence Act and many of the provisions of the Civil Procedure Code and should undergo some judicial training. Without these it would be impossible for them to conduct judicial proceedings.

Power of High Court to Issue Writ of Certiorari Against Income Tax Authorities.

In *Ramjidas Mahaliram In re*, (reported below at page 25), the Calcutta High Court has in an elaborate judgment made some pronouncementswhich may have a very great bearing on the income

tax administration in India. As this judgment is also reported in the authorised law reports of the Government of India (*vide* I.L.R. 62 Cal. 1101), the decision is also of some authority as a precedent. The main proposition laid down in this case is that the High Court has power in a proper case to compel income tax officers (including Assistant Commissioners and Commissioners of Income Tax) to carry out the duty imposed upon them by the law by issuing a writ of *certiorari* or prohibition.

As the question is of vital importance to imcome tax authorities the matter requires their careful attention.

The High Courts have no doubt the power to issue writs of *certiorari* under their Charter; but Section 106 (2) of the Government of India Act provides that the High Court 'may not exercise any original jurisdiction in any matter concerning the revenue' and a writ of *certiorari* can be issued only to 'Courts and Magistrates'.

The Calcutta High Court has got over the first objection on the ground that directing an Income Tax Officer or any Revenue Officer to do his statutory duty is not 'exercising any original jurisdiction in any matter concerning the revenue' within the meaning of the Government of India Act and for this view the ruling of the Privy Council in *Alcock, Ashdown & Co., Ltd.* v. *Chief Revenue Authority, Bombay* (I.L.R. 47 Bom. 742) is relied on. As regards the second objection the learned Judge has held that Income Tax Officers are judicial officers and that the High Court has therefore power to issue a writ of *certiorari* to them. The observations of LORD PHILLIMORE in the Privy Council case to some extent support the Calcutta view, but it has to be noted that what was laid down in that case was only that issuing a direction under Section 45 of the Specific Relief Act to an Income Tax Officer was not 'exercising original jurisdiction in a matter concerning revenue'. Whether issuing a writ of *certiorari* is not exercising original jurisdiction in such matters is open to argument. Apart from this, it is very doubtful whether Income Tax Officers can be regarded as officers exercising judicial functions. Though our personal view is that they are not judicial officers and that the High Court has no power to issue such writs against them, assessees have now to be guided by, and are entitled to take full advantage of, this ruling of the Calcutta High Court and to apply for a writ aginst income tax authorities if they fail to do a duty which

is imposed on them, or purport to do something which they are not empowered by law to do.

We find that our learned contemporary the *Madras Law Journal* is also of opinion that the view laid down in the above said Calcutta case is sound (see 70 M.L.J, Notes p. 1.) So we do not wish to press our view any further.

In a recent case which has not yet been fully reported the Madras High Court has held that the High Court has no power to issue a writ of *certiorari* against a Collector acting under Section 46 (2) of the Income Tax Act but as we have not yet received the full report we are not in a position to know the full details of the case. We shall return to this matter when the judgment is received.

Jurisdiction, to Initiate Proceedings Under Section 34 of the Income Tax Act.

Another question of considerable importance to income tax authorities and assessees is also decided in the above mentioned case (*Ramji Das Mahali Ram, In re*). This relates to the initiation of proceedings under Section 34 of the Income Tax Act (assessment of income which has escaped assessment). The following propositions have been laid down by McNAIR, J., on this subject :—

(1) Unless some item of income has *in fact* escaped assessment or income has *in fact* been assessed at too low a rate an Income Tax Officer has no jurisdiction to start proceedings under Section 34. He cannot act under Section 34 because he merely suspects or 'has reason to believe' that income has escaped. The income must have escaped *in fact*, otherwise, the whole proceedings will be *ultra vires* and void.

(2) It being an essential pre-requisite to reopen an assessment that an item of income must have escaped assessment *in fact* the Income Tax Officer cannot give himself jurisdiction by an erroneous finding of fact that income has escaped. It is not for him to decide whether the preliminary state of facts which give him jurisdiction exists, *i. e.*, whether income has escaped assessment in fact, and if he reopens an assessment without its existence he acts without jurisdiction and it is open to the High Court to issue a writ.

This is also a matter which requires some careful consideration and we shall discuss it in detail in our next issue.

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PROGRESS OF THE LAW OF INCOME TAX IN 1935.

(*Continued from p. 7*)

The rule that no partnership could be legally constituted between a joint Hindu family and a Firm was affirmed in *Prabhulal Peary Lal* v. *Commissioner of Income Tax, Punjab*, (1935 I.T.R. 197) and it was further held in this case that this rule is not confined to registered firms but applies to all kinds of firms. Whether loss incurred by a firm composed of A, B and C can be set off against the income of A and B alone was considered in *Shiv Narayan and Sons* v. *Commissioner of Income Tax, Punjab* (1935 I.T.R 402) and answered in the negative. In *Lal Chand* v. *Commissioner of Income Tax, Bengal* (1935 I.T.R. 330) it was held that prior to the amendment of Section 30 (1) of the Indian Income Tax Act in November 1933 there was no right of appeal from the refusal on the part of the Income Tax Officer to register a firm under the provisions of Section 26-A of the said Act. Their Lordships pointed out in this case that the fact that there is an appeal against the amount of tax under Section 30 (1) and that the question of registration may indirectly affect the amount of tax payable by the assessee could not confer a right of appeal in such a case.

Profits made by a person residing in British India from Foreign Exchange Business have been held not to be assessable to income tax in British India if they are not brought into British India. The Bombay High Court has decided that the, profits in such cases accrue or arise in the foreign countries where the contracts are entered into by the broker and performed, though instructions are given to the broker from British India: *Commissioner of Income Tax, Bombay* v. *Chunilal B. Mehta* (1935 I.T.R, 376). Where the owner of a foreign business advances a loan to an Indian business and subsequently becomes the owner of both businesses and the loan is thus extinguished the question

arises whether there is a constructive remittance of the amount of the loan from the foreign business to British India. This point was answered in the negative in *Meyyappa Chettiar* v. *Commissioner of Income Tax, Madras* (1935 I.T.R. 93). The question whether there is a constructive remittance where a British Indian debt is discharged by the assessee by a hundi drawn on the assessee's business outside British India was considered by the Madras High Court in *L. C. T. C. Subramaniam Chettiar* v. *Commissioner of Income Tax, Madras* (1935 I.T.R. 346). It was held that there is a constructive remittance in such cases but their Lordships pointed out that if the debt itself had been transferred to the foreign business before it was discharged the matter would have been different.

With regard to the assessment of HINDU UNDIVIDED FAMILIES there are some important pronouncements. In *Jupudi Kesava Rao* v. *Commissioner of Income Tax, Madras* (1935 I.T.R. 339) it was held that in the case of a Hindu undivided family if the father dies and the family business devolves on the son by survivorship there is no 'succession' within the meaning of Section 26 (2) of the Income Tax Act and the son is not liable to be assessed as a 'successor' under Section 26 (2).

On the question whether the expression 'Hindu undivided family' is confined to coparcenaries or is wide enough to include a single male member living with female members entitled to maintenance was considered in two cases, namely, *In re Moolji Sicka* (1935 I.T.R. 123) and *Commissioner of Income Tax, Bombay* v. *J. Lakshminarayana* (1935 I.T.R. 367). In the former case it was held that a Hindu undivided family means a Hindu corparcenary but in the latter the Bombay High Court strongly dissented from the earlier decision and clearly laid down that the expression is wide enough to include families consisting of a sole surviving male member and female members entitled to maintenance.

The expression 'sums received as member of a Hindu undivided family' was held to apply to sums received by the brother of the holder of an impartible estate in *Maharaja Visveswar Singh's case* (1935 I.T.R. 216).

Coming to IMPARTIBLE ESTATES the rulings in *Maharani Lakshmibathi Sahiba's case* and *Maharaja Visveswar Singh's case* discuss the question whether the members of an impartible estate

are members of a joint family and whether sums received by them by way of allowance from the family are exempt from income tax under Section 14 (1) of the Income Tax Act. This question is now before the Privy Council and an authoritative pronouncement is awaited.

On the assessment of INTEREST four decisions deserve our notice. The first is that in *Sahu Jagmandar Das's case* (1935 I.T.R. 140) in which interest was held not to be assessable to income tax if it had not in fact been realised, even though it had been credited in the accounts books. This case has to be distinguished from that of *Bhikamchand Lakshmichand* (1935 I.T.R. 120) in which interest was held to be assessable in the case of money deposited with another if the latter credits the depositor with interest in his accounts and informs him of the fact. In *Commissioner of Income Tax, Burma* v. *V. S. U. R. Firm* (1935 I.T.R. 158) and *Commissioner of Income Tax Burma* v. *M.A.L. Chettiar Firm* (1935 I.T.R. 193) it has been held that though the mere execution of a promissory note for interest due may not make the interest assessable as income, yet if the creditor treats the interest as received and includes it in his profit and loss account the income tax authorities would be justified in treating such interest as received and assessing it to income tax. The decision of the Patna High Court in *Dhakheshwar Prasad Narayan Singh* v. *Commissioner of Income Tax, Bihar and Orissa* (1936 I.T.R. 71) in which the Chief Justice differed from the other two Judges shows that the law relating to the assessment of interest which has accrued due but has not been realised is still in a confused state and that much depends on the way in which accounts are kept.

As to NON-RESIDENTS the Privy Council decision in *Currimbhoy Ebrahim and Sons' case* (1935 I.T.R. 395) establishes that the mere advance of a loan by a non-resident to a person carrying on business within British India does not render the borrower an agent of the non-resident for the purpose of receiving interest and that the borrower cannot be made liable as an agent for payment of income tax on the interest paid by him to the non-resident lender. This decision also explains the meaning of the expressions 'business connection' and 'property' in Section 42 of the Income Tax Act.

With regard to service of NOTICES the decision of the Rangoon High Court in *Commissioner of Income Tax, Burma* v. *Dey Brothers*

(1935 I.T.R. 213) may be noted. This case shows that notices must be served in the manner prescribed by Section 63 (1) of the Act. Service on clerks or employees is insufficient and it is also immaterial that the notice has in some way or other reached the person upon whom it was to be served. The essentials of a notice under Section 34 for assessment of income which has escaped assessment are considered in *Jwala Prasad Chobey* v. *Commissioner of Income Tax, Bengal* (1935 I.T.R. 295) and in *Jamnadur Potdar and Co.'s case* (1935 I.T.R. 112) it has been held that 30 clear days' notice must be given from the date of service, for filing a return and that if this minimum period is not given the notice will be illegal and a subsequent extension of time will not cure the defect.

The decision of the Madras High Court in *Muthukaruppan Chettiar's case* that where a retiring PARTNER receives his share of the capital and interest, even the interest paid to him is not assessable, has been reversed by the Privy Council in *Commissioner of Income Tax, Madras* v. *P.R.A.L. Muthukaruppan Chettiar* (1935 I.T.R. 208). The Privy Council took the view which we had expressed in our comments on the case that the principle applied to the distribution of assets in the winding up of companies is not applicable to partnerships.

With regard to RE-ASSESSMENT of income which has escaped assessment and the scope of Section 34 of the Income Tax Act, upon which there is much conflict of opinion there are three decisions deserving notice. *Commissioner of Income Tax, Bombay* v. *G. V. Manohar* follows the decision in *U. Lu Nyo's case* (1933 I T.R. 373) and establishes that proceedings under Section 34 cannot be taken merely because an Income Tax Officer thinks that his predecessor had made a wrong assessment as to income and that in his opinion on the facts the estimate of his predecessor was too low. The other two rulings are *Amir Singh Sher Singh* v. *Commissioner of Income Tax, Punjab* (1935 I.T.R. 171) and *Madan Mohan Lal* v. *Commissioner of Income Tax, Punjab* (1935 I.T.R. 438). In the former case it was held that the section is wide enough to cover any case of non-assessment to whatever cause it may be due, for instance, wrong application of the Act. In the second case it has been held that Section 34 is not confined to cases where income had not been returned at all and that the observations of the Privy Council in *Rajendranath's case* (2 I.T.R.

71) do not lead to any such conclusion. *Dewan Kishen Kishore's case* (1 I.T.R. 143; 14 Lah. 445) in which it was held that Section 34 does not apply to non-assessment due to errors of judgment or misapplication of law stands overruled.

Another question arising under Section 34 namely, whether it is open to an assessee against whom proceedings under Section 34 are taken to re-open the whole assessment and to claim credit in respect of an item which has been over-assessed was answered in the negative in *Madhavji Damodar Thackersey* v. *Commissioner of Income Tax, Bombay* (1935 I.T.R. 457). The scope of this principle is also adverted to in a case decided by the Calcutta High Court, *Jwala Prasad Chobey* v. *Commissioner of Income Tax, Bengal* (1935 I.T.R. 295).

As to REFERENCES the question whether and when a reference lies in the case of best judgment assessment is discussed in detail in *Kesardeo Chamria, In re* (1935 I.T.R. 418). On the respective duties of the assessee and the Commissioner in framing the questions to be referred in *V.S.A.R. Firm's case*, (1935 I.T.R. 61) the Rangoon High Court held that it is the duty of the Commissioner to set out specifically the particular point of law upon which it is sought to obtain a decision from the High Court and deprecated vague and general questions. But in a later case the Bombay High Court held that the assessee is not required to formulate precise questions of law, that the Commissioner is not bound to refer only the questions of law so formulated and that the High Court has power to direct the Commissioner to state a case raising questions of law which have not been formulated before him: *Vadilal Mehta* v. *Commissioner of Income Tax, Bombay* (1935 I.T.R. 152). A similar view was expressed in *Commissioner of Income Tax, Bombay* v. *D. N. Mehta* (1935 I.T.R. 147) in which the same High Court held that the High Court has power to amend the questions referred by the Commissioner and, after raising the real question, to answer it.

The validity of RETURNS signed and verified by agents is considered in *Raja Syed Mahommad Mehdi* v. *Commissioner of Income Tax*, (1935 I.T.R. 202) and in *Jamnadar Potdar and Co.* v. *Commissioner of Income Tax, Punjab* (1935 I.T.R. 112) the Lahore High Court has decided that 30 clear days must be given for the furnishing of a return and if this minimum time is not given the

notice will be illegal and a subsequent extension of time will not cure the defect.

The distinction between SALARY and a lump sum paid in lieu of pension on retirement in consideration of past services is discussed in *Commissioner of Income-Tax, Madras* v. *B. J. Fletcher* (1935 I.T.R. 223). In this case the Madras High Court held by a majority (BEASLEY C.J., dissenting) that the contributions made by a company to the credit of its officers in the Officer's Retiring Fund was not part of the officers' salaries nor a gratuity or profit paid in lieu of or in addition to salary but was a lump sum paid in lieu of pension and was not therefore taxable. The Chief Justice however, held that it was merely an accumulation of bonuses and was assessable.

The true nature of SUBSIDIES paid by the State for payment of the guaranteed interest on the share capital of Railway Companies is considered in *Ahmadpur Khatwa Railway Co., Ltd., In re* (1935 I.T.R. 277); their Lordships have held in this case that such subsidy is income of the company and is liable to be taxed in spite of the fact that it is intended to be paid automatically to the shareholders and that the guaranteed interest payable to shareholders is not deductible as interest on borrowed capital.

The scope of the exemption relating to TRUST PROPERTY is discussed in detail in *The Tribune Case* (1935 I.T.R. 246) in which it was held that the income of *The Tribune*, a newspaper which a philanthropist had founded by his will for the benefits of the public was not income from property held under trust for charitable purposes and was not entitled to exemption from income-tax.

In the above review we have only dealt with the more important judgments. For decisions of minor importance reference may be made to our Annual Digest of Income-tax Cases for the year 1935.

Separation of Hindu Family : Finality of Order under Section 25-A (1) :

When an Income Tax Officer finds after enquiry that the members of a Hindu undivided family have separated and registers the members as a firm, is it open to him or his successor in a subsequent year, when an application is made for renewal of the certificate of registration, to make a fresh enquiry and refuse renewal of registration on the ground that the previous finding that the members had separated was wrong and that no separation had in fact taken place ? This important question was raised before the Judicial Commissioner's Court of Nagpur in *Sir Biseswar Daga's case* (reported below). In this case an Income Tax Officer thought that the finding of his predecessor that the members of Sir Biseswar Daga's family had separated was erroneous and after making a fresh enquiry refused to renew the certificate of registration as a firm, holding that no separation had in fact taken place. On a reference by the Commissioner the Judicial Commissioner's Court held that the proceedings taken by the second Income Tax Officer were wholly illegal. The learned Judges said that once an order under Section 25 A (1) of the Income Tax Act has been passed by an Income Tax Officer after enquiry it is not open to him or to his successor to go behind this finding. Such a procedure, in the view of the learned Judges, is contrary to the provisions of sub-Clause 3 of Section 25-A and Rule 6 of the Income Tax Rules. Under Rule 6 it is incumbent on an Income-tax Officer to renew a certificate of registration from year to year on an application made to him in that behalf accompanied by a certificate signed by one of the partners that the constitution of the firm remains unaltered.

Inasmuch as an order made under Section 25-A (1) is thus final Income Tax Officers would be well advised in making a detailed enquiry into the fact of separation before making an order under that section. An enquiry of a perfunctory nature leaving matters to be enquired into more closely in future years as was done in *Sir Bisweswar Daga's case* should be avoided.

Reference From Application for Refund.

The interesting question whether an application for a reference can be made to the High Court in respect of an order on an application for refund under Section 48 of the Income Tax Act arose for decision before a recent case in the Rangoon High Court in *Adamji*

Hajee Dawood & Co., Ltd. v. *Commissioner of Income Tax, Burma* (to be reported shortly) and it was held that as Section 66 (3) of the Act is controlled by Section 66 (2) and under Section 66 (2) an assessee is not entitled to require the Commissioner to state a question of law arising out of an order under Section 48 an assessee is not entitled to apply to the Court under Section 66 (3) to require the Commissioner to state a case and refer the question which the assessee seeks to have answered. This decision reveals a defect in the Act. Very complicated questions of law often arise in the matter of refund and there is no reason for not providing for a reference to the High Court in such cases.

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NOTES & COMMENTS.

Assessment of Talkies.

An interesting question relating to the assessment of cinemas was recently raised in the case of *Hakim Ram Prasad*, (reported below at page 104). The assessee, a cinema proprietor of Lahore, installed an electric company's sound projector equipment under an agreement which provided that the assessee should have the use of the projector for 10 years, that he should keep the equipment in order, that the company should have access to the machine for making adjustments and repairs and that, at the expiration of the agreement, the machine should be handed back to the company. The machine was to remain at all times the sole and exclusive property of the company throughout the 10 years and at the termination of the agreement. The assessee agreed to pay Rupees 41,856 in the first year and Rupees 4,800 for each of the subsequent years in addition to an initial payment of Rupees 10,950. In assessing the income from his business the income tax authorities refused to deduct the sum of Rupees 41,856 paid for the first year holding that it was in the nature of a capital expenditure and not rent and that it was not therefore deductible from the profits for that particular year. The High Court of Lahore (Sir DOUGLAS YOUNG, C.J. and MUNROE, J.) held that, on the face of the agreement it was clearly an ordinary renting agreement, and that there were no materials for holding that the sum paid was not in the nature of rent. Their Lordships further said that the fact that the lessor took half the total rent in one year and the rest of the rent was spread over nine years did not lead to any inference that the payment in question was a capital investment.

As the learned Chief Justice has pointed out, there may be cases where it would be possible to dissect the amount nominally paid as rent and to hold that the payment, or a portion of it, is a capital investment. But for this there must be sufficient facts. If for example it were proved that the lessee was really paying in the course of ten years the total value of the machinery and that

the machinery would be of no value at the end of ten years, the Court could probably come to a decision that the whole expenditure was in the nature of capital except such amount which would have to be allowed as interest. On the other hand, it may very well be that the total payment over the ten years is only a fair rent of the machinery during that period and that further the value of the machinery at the end of the ten years may be quite a substantial amount. The question is one depending upon the facts but if the agreement on the face of it is an ordinary renting agreement as in this case and there is no evidence to show the contrary, the income tax authorities would not be justified in refusing to deduct the amounts paid to the lessor company.

Refund of Tax on Dividends : A Hard Situation.

The case of *Adam Hajee Dawood and Co., Ltd.*, decided by the Rangoon High Court and reported below at p. 100 reveals a defect in Section 50 of the Income Tax Act which as it stands operates harshly on assessee. Section 48 of the Act, contains a provision for refund where income tax has been levied on dividends at a higher rate than the rate applicable to the total income of the shareholder. It is obvious that it is impossible for an assessee to ascertain whether or not he is entitled to a refund under Section 48 (1) until the assessment has been made upon him but Section 50 provides that an application for refund under Section 48 must be made within one year from the last day of the year in which the tax was recovered or before the last day of the financial year commencing after the previous year, irrespective of whether an assessment has been made on the assessee or not. Further though that section, (*viz.*, Section 50) expressly provides that a claim for refund under Section 49 may be admitted after the period of limitation if there is sufficient cause, it does not contain any similar provision with respect to a claim for refund under Section 48. The High Court of Burma has decided that as the law stands at present there is no power to entertain a claim for refund after the expiry of the one year prescribed, even though the assessment has been made on the shareholder's income and he is placed in a position to claim a refund under Section 48 only after the expiry of that year. The learned Chief Justice (Sir ARTHUR PAGE, C.J.) has point out that the remedy lies with the legislature not with the Courts and we hope that the persons concerned will take the advice of the Chief Justice and bring the matter to the notice of the Government.

Assessment of Liquor Shops :

A question of some practical importance relating to the assessment of liquor shops was decided in a case which came up before the Bombay High Court and is reported below at p. 95: *Hirabai D. Desai & Sons* v. *Commissioner of Income Tax, Bombay.* In this case the assessee who carried on liquor trade kept his accounts not on the cash basis but by entering the amount of liquor purchased and charging the market price for the day for the amount by which the stock of liquor was diminished that day. The Income Tax Officer refused to adopt this method of accounting as a system from which the assessee's income could be correctly deduced and, applying the provisions of the Proviso to Section 13 of the Income Tax Act, computed the income adopting another basis. He also added a sum of Rupees 42,000 odd in respect of what is called *kasar*, *i.e.*, selling by short measure, on the ground that it is a well-known fact that all liquor sellers of the locality sold at short measure and that the assessee must be taken to have adopted this practice. The High Court held, on the first point, that, as the method adopted by the assessee would not indicate the true income if the liquor had been sold at short measure, the Income Tax Officer was entitled to reject that basis and to adopt a basis which he considered more reliable; but their Lordships pointed out that if the Income Tax Officer adopts his own method he must show the basis on which he arrived at the true income.

Illegal Practices Cannot Be Presumed :

The second point decided in the above mentioned case which is also of considerable importance, is that the Income Tax Officer was not entitled to presume without any evidence that the assessee had also adopted the practice of selling by short measure merely because most of the liquor traders adopted such an illegal practice. The principle of this decision is not confined to liquor trades but is of general application. Though various kinds of illegal practices are often resorted to by traders, this ruling shows that it is not open to income tax authorities to presume that the trader who is being assessed must have adopted such a practice. It is one of the rudimentary principles of law that the law will not presume the commission of an illegal or criminal act. The presumption is always in favour of innocence.

Payments to Wife: No Presumption What Wife is Only Husband's Benamidar.

In *Ram Kinkar Banerjee* v. *Commissioner of Income Tax, Bihar & Orissa* (reported below at p. 108) a question which, though a short one, is of extremely great importance in India has been decided by the Patna High Court (Sir COURTNEY TERRELL, C. J., and MOHAMMED NOOR, J.) When an Income Tax Officer finds in the assessee's accounts entries of payment made to the assessee's wife the question arises whether he can presume that the wife is only the husband's *benamidar* and that the payments are really made to the assessee himself? In the above said Patna Case, the husband who had an interest in a colliery made a payment of Rupees 15,000 odd as royalty to his wife who had acquired the rights of the superior landlord, but the Income Tax Officer, treating the lady to be the assessee's *benamidar*, refused to allow him to deduct this amount from his income. The Commissioner upheld the assessment, holding that, as there was no evidence that the wife acquired this right with her own funds, it was reasonable to presume that the right in question was acquired by the husband in the name of his wife. The High Court held that this view was erroneous.

The learned Chief Justice said "there being therefore no dispute that the property stands in the name of the lady, she must be taken to be the owner of it unless there is any evidence to show that she is a *benamidar*............There is no presumption that a property standing in the name of a married Hindu lady does in fact belong to her husband. The ordinary presumption of law is that the apparent state of affairs is real unless the contrary is proved. The absence of evidence one way or the other did not under the law justify the Assistant Commissioner in drawing the inference that the lady was a *benamidar* of the husband".

Profits From Rearing of Animals, Whether Income from Property or Income from Business.

[*Where animals are reared in farms and income is derived from the sale of such animals the question arises whether such income is income from property or income from business. The* Law journal of England (*February 1, 1936*) *contains the following learned article on this subject.*]

WHETHER a silver fox farm was assessable under Schedule B or Schedule D, and if it was assessable under Schedule B, whether, further, the occupation of the land was not for the purposes of husbandry only or mainly for those purposes, were questions of interest that were recently raised in the Scottish case of *Inland Revenue Commissioners* v. *Melross* (1935, 23 R. and Income Tax 103). In such cases it is not always easy to determine whether there is an occupation of the land which is assessable under Schedule *B*, or whether in fact the profits are really the profits of a trade assessable under Schedule *D*.

It is also to be observed that in cases where Schedule B is the proper schedule, the assessment, having regard to the definition of "assessable value" in Schedule B, will only be on one-third of the annual value when the occupation of the land is not for the purposes of husbandry only or is not mainly for those purposes.

The material facts in *Inland Revenue Commissioners* v. *Melross* were as follows:

The respondent was the tenant of some 55 acres of land, on the greater part of which he kept a poultry run and also grew vegetables. On 14 acres of this land he had a silver fox farm. One half of these 14 acres were used for breeding pens, while the other half were used as open runs for exercising the foxes.

Although a silver fox is a carnivorous animal, at the same time it needs a substantial amount of vegetable produce. And the foxes on this farm consumed grass, watercress, spinach, lettuce, carrots and potatoes, which were grown on other parts of the holding. Moreover, in the breeding season the vixens and the cubs consumed a considerable quantity of eggs, which also were produced on the holding.

The Commissioners held on these facts, notwithstanding that substantial profits were derived from the sale of the foxes, that there was an occupation of land assessable under Schedule B, and

that no assessment could be made on the basis that there were profits arising from a trade. They further held that the occupation was not solely nor mainly for the purposes of husbandry, and that accordingly the assessment under Schedule B was to be made on one-third of the annual value.

It may be as well to examine previous decisions, in order to see what principles, if any, are deducible from the authorities. It is important to remember, however, that the determination of such questions is one of fact and of degree, and that as long as there is some evidence in support, a decision arrived at by the Commissioners will not be interfered with on appeal.

If guidance was desired as to the nature of the profits from the occupation of land which are assessable under Schedule D, one cannot do better than refer to LORD WRIGHT's judgment in *Glanely* v. *Wightman* (1933, A.C., 638 ; 1 I.T.R. 225), where it was held that the fees in respect of the services of a stallion on the stud farm, which stallion never left the farm, but was visited by mares of other owners, were profits in respect of the occupation of the farm, and were not accordingly assessable under Schedule D.

In his judgment in that case, LORD WRIGHT said ;

" Profits of ' occupation ' include gains from the animal produce as well as the agricultural, horticultural or arboricultural produce of the soil. And the references to gardens, nurseries and woodlands show a scope of Schedule B beyond the use of the land and its products for the provision of food ; equally, it is obvious that the rearing of animals, regarded as they must be as products of the soil—since it is from the soil that they draw their sustenance and on the soil that they live, is a source of profit from the occupation of land, whether these animals are for consumption as food (such as bullocks, pigs or chickens) or for the provision of food (such as cows, goats or fowls), or for recreation (such as hunters or racehorses), or for use (such as draught or plough horses). All these animals are appurtenant to the soil, in the relevant sense for this purpose, as much as trees, wheat crops flowers or roots, though no doubt they differ in obvious respects. The farmer is still dealing with the produce of the soil, and Schedule B covers the income."

No doubt the carrying on of such operations as that of a stud farm, a silver fox farm, the growth of produce with a view to sale, and the like, are strictly trading operations and amount to the carrying on of a trade, in the normal sense; but for tax purposes,

where such a trade is exercised by the occupation of the land itself, it constitutes a profit of the land which properly falls to be assessed on the annual value basis under Schedule B and not on the profits basis under Schedule D.

Thus, in *Back* v. *Daniels* (1925, 1 K. B. 526), it was held that the profits derived from the sale of potatoes grown on land hired for the purpose by potato merchants were profits from the occupation of land, assessable under Sched. B and not under Sched. D.

As SCRUTTON, L. J., pointed out:

" Cultivating land to grow produce for the purpose of sale is ......a trade. But Parliament has dealt with that trade where it is exercised by the occupation of land by assessing the occupier on the annual value of the land and not on the profits made out of its produce......"

An assessment on the profits basis under Schedule D can only be made in such cases, in so far as there may be some distinct operation unconnected with the occupation of the land, such as a butcher s shop dealing with the beasts of a cattle farm, or the service by a stallion of mares belonging to other owners away from the stud farm where the stallion is kept: *Malcolm* v. *Bockhart* (1919, 35 T.L.R. 231). Contrast *Glanely* v. *Wightman* (*supra*).

As regards decisions on poultry farming, reference may be made to *Lean and Dickson* v. *Bull* (1925, 10 Tax Cas. 341); and *Jones* v. *Nuttall* (1926, 3 R. and Income Tax 242; 10 Tax Cas. 346).

In the former case there was a combined business of poultry farming and tomato growing on the land, which was 33 acres in extent, with the exception of half an acre on which green food for the poultry in winter was grown. The land was wholly grass, and was used by the poultry and a small flock of sheep in common.

It was held that the land was occupied for the purposes of husbandry, since the trade or business carried on depended to a material extent on the industrial or commercial use of the fruits (natural or artificial) of the land.

As LORD CLYDE put it (10 Tax Cas. at p. 345):

" While the use of the fruits of the land in the trade or industry carried on upon the land is vital to bring that trade or industry within the description of husbandry, my opinion is that it is enough

that those fruits are to a material extent used in such trade or industry."

Jones v. *Nuttall* is even a stronger case, since all the food for the poultry was bought, and since there was not such an extensive use of the "fruit" of the soil for the nourishment of the poultry or any other animals.

The distinction between a case falling under Schedule D and one falling under Schedule B is well expressed by ROWLATT, J., (at p. 349):

"If you have land which is used really as so much space for such creatures (as chickens, etc.) to exist upon, then it is as much Schedule D as if you kept a stable full of horses or a byre or pasture full of cows that were fed and kept there......But where you get stock, whether it is fowls or anything else, which materially live upon the fruits of the soil, vegetable fruits, insect fruits, and I dare say mineral fruits, too......then it is right and proper to treat the profits from that sort of enterprise as being husbandry and within Schedule B."

If one applies these principles to the *Melross* case, where a silver fox farm was kept, the foxes lived to a material extent upon the "fruits" of the land on which they were kept, and the trade was one arising from the occupation of the land itself, and did not constitute a separate enterprise unconnected with occupation. In the circumstances, accordingly the profits were assessable under Schedule B.

But the principal operations there carried on did not constitute husbandry, since the term "husbandry" contemplates some sort of operation intended directly or indirectly for the support of human life, such as the direct or indirect production of food for human consumption, though it has also been held to extend to the production of medicines and drugs for human consumption: *Inland Revenue Commissioners* v. *Ransom, Ltd.* (1918, 2 K.B. 709); to sheep grazing: *Keir* v. *Gillespie* (7 Tax Cas. 473); and to poultry farming: *Lean* v. *Bull; Jones* v. *Nuttall* (*supra*).

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NOTES & COMMENTS.

Judicial Committee on the Assessment of Firms.

The Judgment of the Judicial Committee in the case of *Rm. Ar .Ar. Rm. Arunachalam Chettiar* reported at page 173 contains some pronouncements of great importance relating to the assessment of partners.

In the first instance it firmly establishes the principle laid down in *Commissioner of Income-tax, Madras* v. *Rm. Ar. Ar. Arunachalam Chettiar* (I. L. R. 47 Mad. 660) that a partner in an unregistered firm which has made a loss in the year of account is entitled to set off his share of the loss against the profits and gains made by him in his individual trade and otherwise. Their Lordships have fully approved of the decision in the abovesaid case and of the reasons given in the judgment of SIR WALTER SCHWABÉ, C.J. In particular their Lordships are of opinion that the learned Chief Justice rightly rejected the contention put forward in that case that an unregistered firm was for income-tax purposes an entity or that the same person as an individual and as a partner of a firm is two separate entities merely because the business of the firm is a separate business and the firm is treated as an assessee. Their Lordships have clearly laid down that in their opinion whether a firm is registered or unregistered, partnership does not obstruct or defeat the right of a partner to an adjustment on account of his share of loss in the firm whether the set-off is against other profits under the same head of income within the meaning of Section 6 of the Act or under a different head, in which case only need recourse be had to Section 24 (1)

Questions more complicated and difficult arise when a partner has paid more than his share of the loss of the firm, owing to the inability of the other partner to pay. Their Lordships are of opinion that in such a case, though logically it may perhaps be said that the whole of the loss of the last year of trading is falling upon one partner and not merely his proper share of the loss, yet for income tax purposes very different considerations arise. A partner cannot at the end of any year's trading claim to set off the whole of the firm's loss in the previous year treating the other partner as insolvent, nor can he do so on the dissolution of the firm. He

cannot, even later, according as the other partner's insolvency becomes established, set off in one year the whole of such partner's shares of losses for serveral years. The opinion of the Judicial Committee is clearly expressed and is final and there is no use of dwelling upon the misconceptions on which the judgment is based. But there is still a ray of hope, though a distant one, for those who think with us that this view is unsound. The assessee in the case in question by making certain entries in his accounts made a claim only as a bad debt due by his partner and did not as their Lordships themselves have stated "in his character of partner formulate any claim to a deduction of more than his share of the loss," and the observations of the Judicial Committee on this part of the case are only *obiter dicta*. When an assessee expressly formulates a claim *in his character of partner* to a deduction of more than his share of the loss of the firm the matter may perhaps have to be gone into more fully by the High Courts of India and the Judicial Committee.

A Clever Device to Evade Income Tax.

In a recent case the assessee's accounts were kept on the cash basis and the real nature of certain payments received by him towards interest was obscured by clever cross entries, and these payments escaped the attention of the Income Tax Officers who assessed him for the years in which the payments were made. When the principal amount was finally paid to the assessee the then Income Tax Officer added up all the sums received from the debtor and considered the difference between the amounts thus received and the amount of the loan as income received in the year in which the debtor's accounts finally closed. Their Lordships said that the procedure was not justified by law. It was a case not of receipts kept in suspense but payments received and allocated towards interest but obscured by clever cross entries. If the income-tax authorities were not able to detect the true nature of the entries, it would be their own fault and this would not entitle them to assess an income which was not received in the year of account. (Vide *Ratanchand Lallumal, In re*).

Assessee's Right to get copy of 'opinion' of Commissioner.

In the above mentioned case (*Ratanchand Lallumal, In re*) the Allahabad High Court has held that under the Rules of the said High Court an assessee who is applying for a Reference to the High Court under Section 66 is entitled to get only a copy of the 'statement of the case,' made by the Commissioner and that he is

not entitled to get the opinion of the Commissioner. If this interpretation of the rules is correct we think, the rule should immediately be amended so as to make provision for a copy of the entire statement of the case including the opinion of the Commissioner to be given to the assessee, for obvious reasons.

Allowance of Interest Paid to Partners on Capital Contributed.

In *Commissioner of Income Tax, Bombay* v. *Tejbhandas Motumal* [1933 I. T. R. 202] it was decided by the Judicial Commissioner's Court of Sind that where a capitalist partner contributes capital to the firm on condition that interest should be paid to him the firm is entitled to claim an allowance for the interest paid on such capital. It was further observed in this case that it was immaterial whether such capital was advanced as initial capital or subsequently and that it was not possible to draw any distinction between capital borrowed and capital contributed. "Capital contributed by a capitalist partner" the learned Judicial Commissioners said, "is capital borrowed from him by the firm." In commenting upon this case we said that there is a fundamental distinction between a contribution and a loan, that contribution does not necessarily imply a loan and that it is not correct to say that capital contributed by a partner is necessarily capital borrowed from him by the firm. We pointed out further that in order that interest may be allowed under Section 10 (2) (iii) it is not sufficient that it is not made dependent on the earning of profits. There is the further and more important condition that the capital must have been *borrowed* and whether an advance made by a partner is a contribution of capital to the firm or a *bona fide* borrowing of money by the firm in which the lender happens to be a partner is a question of fact in each case.

We find from the recent judgment of the Judicial Commissioner's Court of Sind reported at page 227 *infra* that the Judicial Commissioners have refused to grant leave to the Commissioner to appeal to the Privy Council from the above said judgment. It has, however, to be noted that their Lordships have receded to some extent from the broad statement made in the previous judgment. Their Lordships now say that the observation that it is not possible to draw any distinction between capital borrowed and capital contributed, that it is only a different way of expressing one and the same thing and that the capital contributed by a capitalist partner is capital borrowed from him by the firm, must be read along with the preceding paragraph and that that paragraph makes it

abundantly clear that if the conditions of Section 10 (2) (iii) ar complied with, nothing turns upon the use of the expressio money contributed by a partner as opposed to the expression mone borrowed from a partner. Certainly, if the conditions of Sectio 10 (2) (iii) are satisfied there is no difficulty at all, but these ques tions arise only when we have to decide whether the condition of Section 10 (2) (iii) are satisfied.

Anyhow, as the learned Judicial Commissioners have affirme the decision it would certainly be of great advantage for partner especially those residing in Sind to follow the example of the firn Tejbhandas Motumal in drawing up clauses relating to contribu tion in partnership deeds. Under this decision if A and B agree tc contribute Rs. 100 each without interest and Rs. 10,000 each with interest thereon at a certain rate, the interest received by them on Rs. 10,000 each can be deducted from the profits of the firm as interest on borrowed capital. The capital to be invested without interest may be a nominal sum. It is however a matter to be noted that the learned Judicial Commissioners have observed that it was perhaps possible for the learned Commissioner to have so framed this question as to make it a question of general importance. As the question is obviously one of very far-reaching importance we hope that when the question next arises the Commissioner would frame the question in such a way as to show its importance and take up the matter to the Privy Council.

Power of High Court to Order Payment of Costs of Appeal to Privy Council Irrespective of Result of Appeal.

The learned Judicial Commissioners have made an important suggestion in this case which deserves the careful attention of the legislature. In was decided by a Full Bench of the Madras High Court that if the amount involved in an appeal to the Privy Council is very small but the principle involved is great the High Court can refuse leave to appeal unless the appellant agrees to pay the costs of the appeal irrespective of its result. As the learned Judicial Commissioners have pointed out in this case: "In nine cases out of ten the decision given against an Income Tax Commissioner becomes a decision of importance as between him on the one hand and the assessees in general on the other. The pecuniary amount involved in most of these cases is small and it is difficult for the assessee concerned in a particular case to incur the expense of appearing before their Lordships of the Privy Council." The learned Judicial Commissioners have expressed a

hope that the legislature will consider the advisability of conferring a power upon the High Courts to impose a condition in a fit case at the time of granting leave to appeal to the Privy Council in cases falling under Section 66 A of the Income Tax Act that whatever may be the result of the appeal the appellant should pay the costs of the other party as between solicitor and client.

The Judicial Committee Affirm the Hungerford Investment Trust Case.

The decision of the Calcutta High Court in *The Hungerford Investment Trust* case which was reported by us last year (see 1935, 3 I.T.R. 188) has been affirmed by the Privy Council and so long as the Indian Income Tax Act is not amended in this respect shareholders of companies carrying on business outside India can freely enjoy foreign income in India without paying Indian income tax. If foreign income is brought as such into India income tax will be levied, but the entire income of a company including foreign income can be distributed in India in the form of dividends without paying Indian income tax. Shareholders in companies carrying on trade in foreign places thus enjoy an anomalous advantage which is denied to members of an ordinary partnership. It may be worth while for firms carrying on business outside British India and having much foreign income to see if by registering themselves as a private company they cannot bring themselves within the ruling in the *Hungerford Investment Trust Case*, and thus save themselves from the clutches of income tax. The judgment of the Privy Council is reported at page 270 below.

Sir David Yule's Estate Case.

The decision in *Sir David Yule's Estate Case* [1935, 3 I.T.R. 163] has also been affirmed by the Privy Council. The judgment of the Judicial Committee establishes beyond doubt that if the accumulated profits of a company are capitalised and distributed as bonus debentures to the shareholders, the shareholders do not thereby receive any income and they cannot therefore be assessed to income-tax in respect of the amount received in the shape of debentures. If a company unreasonably delays the declaring of dividends and accumulates its profits there is a provision in the Indian Income-tax Act which authorises the income-tax authorities to levy income-tax on the proportionate share of each member in the profits and gains of the company [see Section 23-A]. But by issuing bonus debentures to the shareholders companies can escape

the provisions of Section 23-A and the decision in *Sir David Yule's Case* is one which companies should be well aware of.

The Judicial Committee have further taken care to point out with some emphasis in their judgment in this case that provided there is in fact a capitalisation of the accumulated profits, the personal motive or purpose of the individual shareholders, even if they hold a controlling interest in the company is irrelevant.

Assessment of Person Keeping Different Accounting Periods for Different Businesses.

The judgment of the Bombay High Court in *Commissioner of Income Tax, Bombay* v. *Abubaker Abdul Rahman* reported *infra* at page 233 deals with a question of considerable importance relating to the assessment of persons carrying on different businesses. With regard to whether a person can keep different accounting periods for different businesses, their Lordships say that an assessee who carries on two different businesses cannot make up his account for the different businesses in such a way as to give him two separate previous years ending in different dates for the purpose of income-tax, but there is no reason why an assessee should not fix one date for his individual business and a different date for a firm of which he is a member with others, inasmuch as a firm is a distinct assessable unit. If an assessee is thus entitled to keep two different dates one for himself and another for his firm, the question arises as to how he is to submit his return and how he is to be assessed. In the case in question the assessee fixed for himself as the previous year the year ending November 9, 1938, whilst a firm in which the assessee was a member fixed as its previous year the year ending December 31, 1931. In 1932-1933 he submitted a return showing his individual income only and was assessed upon it. His share in the profits of the firm was determined on December 31, 1931, and the Income Tax Authorities after assessing the income of the firm, sought to treat the assessee's share in such income as having escaped assessment for the purpose of levying super tax on the assessee. The High Court held that in making a return of his total income down to November 9, 1931, the assessee was not bound to include his share in the profits of the firm which were ascertained only after December, 1931. He was only liable to tax in respect of the income of the year which ended on November 9, 1931, and the profits to which he was entitled from the firm must necessarily fall within the next year of assessment, i. e., the year from November 10, 1931, to November 9, 1932.

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Fees Paid to Directors of Private Companies.

LAKSHMI NARAYAN SEN AND SONS' CASE.

The decision of the Calcutta High Court in *Lakshmi Narayan Sen & Sons, Ltd., In re* (reported in this issue) deals with a question of far-reaching importance to directors of Companies. While on the one hand, if the decision is properly understood and applied it would only prevent companies from intentionally evading income tax or super tax by distributing their profits in the guise of allowances or fees to their directors, if the exact scope of the decision and the principle underlying it are not properly appreciated, it is liable to be misapplied in such a way as to enable the income tax department to interfere with the citizen's freedom of contract and the businessman's right to manage his business and pay his servants according to his discretion.

The articles of association of a private limited company consisting of three shareholders who were also the directors of the company empowered the directors to draw an allowance and the directors drew Rs. 600 each per month. The income tax authorities on enquiry found that Rs. 175 per month would be a reasonable remuneration for the services rendered by the directors and that the amount of Rs. 600 was drawn by them not as *bona fide* remuneration for their services but as a mere device for minimising the company's profits with a view to enable the company to escape super tax, and refused to allow as business expenditure the excess drawn by the directors over and above Rs. 175 each per month. The High Court held that the question whether a certain expenditure was expenditure incurred solely for the purpose of earning the profits within the meaning of Section 10 (2) (ix) of the Indian Income Tax Act was a question of fact and, as the Commissioner had found that the excess over Rs. 175 per

month was not incurred solely for earning the profits, the High Court would not interfere. It was further of opinion that it was competent to the income tax authorities to ascertain whether the payments were *bona fide* payments or a mere device for the purpose of evading payment of income tax or super tax and this was also a question of fact.

SCOPE OF THE DECISION.

It is of the utmost importance that the true principle underlying this decision and the exact scope of the powers of the income tax authorities in this respect should be well defined and understood. A case almost on all fours decided by the Judicial Commistee in 1932 and reported in 1932 A.C. 683, 101 L.J.P.C. 177 and 1932 Comp. Cas. 541 (but which does not appear to have been brought to the notice of the Calcutta High Court), *Aspro Ltd.* v. *Commissioner of Taxes*, is reprinted by us in the current issue of our *Income Tax Reports*, as it is a decision of the highest authority and throws more light on the subject, and we hope when the matter comes up again before the High Courts of India these powers will be defined more precisely than in *Lakshmi Narayan Sen & Son's Case.*

The decision in *Lakshmi Narayan Sen & Son's Case* should not be understood as laying down that where directors have received allowances or salaries and the income tax authorities think that the allowances or salaries are high, they have the power to make an enquiry as to what would be a reasonable remuneration and to allow as business expenditure only such amount as they think reasonable. The Company on the one part and the Directors on the other are the proper persons to decide what should be the proper remuneration for the directors and the income tax officers have no power to substitute their own discretion for that of the parties concerned. They have no jurisdiction to override the company's right to decide what should be paid as remuneration to the directors. Their duty is only to find out whether the payments made are or are not genuine and *bona fide* payments of remuneration, and if they are genuine and *bona fide* payments made towards remuneration, the income tax authorities must allow them as business expenditure even though in their opinion the amount fixed is extraordinarily high. In other words, under

Section 10 (2) (ix), the income tax authorities have no right to say that the assessee *ought not to have incurred* so much expenditure by way of remuneration of directors and that they will allow only so much as they think reasonable on enquiry. They can only say that the assessee *has not in fact and in truth incurred* so much expenditure by way of remuneration of directors. The excessive nature of the remuneration is not in itself a ground for cutting it short but is only a matter which, combined with other circumstances, may lead the income tax officers to a finding that the payments made to the directors were not *bona fide* payments for remuneration but in truth a distribution of the profits. The distinction though fine is a substantial one.

The correct principle can be gathered from the following passage in the judgment of LORD THANKERTON in *Aspro Limited* v. *Commissioner of Taxes* cited *supra*):—

"The appellants maintained in the second place that the Commissioner was not entitled to challenge the amount paid by the company to its servants for their services on the ground of excess or over-generosity in its amount, for that was entirely a matter in the discretion of the company, and that he could only challenge the payment on the ground that it was not a genuine transaction being in fact fictitious, or the sums so paid being wholly, or partly, not truly paid as remuneration for their services. . . . . The respondents substantially accepted the premises of this contention."

Pension Paid Outside British India to Persons Residing in India.

SIR T. VIJAYARAGHAVACHARYA'S CASE.

A notification issued under Section 60 of the Indian Income Tax Act exempts from Indian income tax pay, leave salaries, and pensions paid outside India *to persons residing out of India* : (See Income Tax Manual p. 156). What about pay, leave salaries and pensions paid outside India *to persons residing in India* ? *Prima facie* it would seem that the maxim *expressio unius exclusio alterius* would apply to a case like this and that such payments made to persons residing in India are not exempt from Indian income tax. But the Lahore High Court, after an elaborate consi-

deration of the question, has come to the conclusion that even in the case of persons residing in India, pay, leave salaries and pensions paid outside India, cannot be assessed to income tax in British India. Under Section 4 (1) of the Indian Income Tax Act only such income as accrues or arises or is received in British India can be assessed to income tax in India. In their Lordships' opinion, income does not accrue or arise where it is earned or where the source of the income is situated, but where there is a right to demand payment of it or where it is in fact paid. Under the Civil Service Rules where pension is payable in rupees it is payable at any treasury in India or at the pensioner's option at the Home Treasury. Where the pensioner exercises his option to receive his pension in England as in this case it accrues or arises in England and is not therefore assessable under the Indian Income Tax Act. The notification made under Section 66 is in their Lordships' opinion superfluous. It appears from the judgment that Mr. Sundaram in his *Law of Income Tax* is also of the same view.

Is the Decision Sound?

The observations of Mr. Justice Mukerji in *Rogers Pratt Shellac & Co.'s case* (I. L. R. 52 Cal. 1) and of Mr. Justice Ormiston in the case of *Phra Phraison Salarak* (I. L. R. 6 Rang. 598) which have been strongly relied upon by their Lordships, when read carefully and along with the facts of the cases are not only not 'decisive of the present case' but do not even support the conclusion of their Lordships. Mr. Justice Mukerji distinctly says that the words 'accrue or arise' refer to a stage *anterior* to the point of time when the income becomes receivable. This is no authority for the view that income accrues where it becomes receivable but supports the view that it may accrue at one place and become receivable at another. What Mr. Justice Ormiston held in the Rangoon case was that where a Siamese Government Official did some work for the Siamese Government in Burma, his pay did not accrue or arise in Burma. The inference from this decision is that even if Sir T. Vijayaraghavacharya had worked in England his pay would have accrued in India. This case also does not support the view taken by the Lahore High

Court. The decision of the Allahabad High Court in *In re Saunders* (I.L.R. 54 All. 223) is a much stronger case than the present one. There the Fund out of which the allowance was paid to the Bishop of Lucknow was in the United Kingdom and the allowance was payable only in the United Kingdom. Still it was held that the income accrued in India as it was paid to the assessee as Bishop of Lucknow. Sir T. Vijayaraghavacharya's case seems to be a typical instance of income which 'accrued or arose' in British India but was 'received' outside British India. In our view even apart from the inference from the notification, the weight of authority as well as principle is in favour of the view that pay, leave salaries and pensions paid outside India, to Indian Civil Servants residing in India accrue or arise in India, and we await with great interest the opinion of the other High Courts on this important question.

There is also another aspect of this case to which their Lordships' attention does not appear to have been drawn. Where a salary or pension is receivable at A, B or C according to the assessee's option, it does not necessarily accrue at the place where the assessee, exercising his option, receives it. It can accrue at place A and yet may be receivable at B or C. The fact that the assessee had an option to receive his pension at London and did receive it there does not necessarily lead us to the conclusion that the income accrued at London.

If the view propounded in this case as to the meaning of '*accrue or arise*' is correct, foreigners who enter into contracts of service and serve in India, cannot be assessed to Indian income tax in respect of their salaries, if they make it a condition of the contract of service that their salary should be paid by their employers into a Bank outside British India to their account.

'Annual Value': Whether Includes Municipal Tax Paid by Tenant: A Full Bench Ruling.

In the year 1931 the Lahore High Court decided (by a majority) in *Chunnamal Saligram* v. *Commissioner of Income Tax, Punjab* (131 I.C. 193; A.I.R. 1930 Lah. 320) that the term 'annual value' in Section 9 of the Indian Income Tax Act meant the annual money benefit derivable from the property by the landlord and that

where property is leased out to a tenant for a fixed rent and the tenant is also directed to pay the municipal tax, the amount of municipal tax payable by the tenant is not to be included in fixing the 'annual value' of the property for the purpose of assessing its owner to income tax. In the next year the same question arose before the Calcutta High Court in *Krishna Lal Seal In re*, [1932, I.L.R. 60 Cal. 357]. The learned Judges who heard the case dissented from the ruling of the Lahore High Court in *Chunnamal Saligram's Case* and the reasoning on which it was based. Owing to this conflict of judicial opinion the matter was again referred to a Full Bench of seven Judges by a Division Bench of the Lahore High Court in a recent case reported at p. 250 infra (*Lalla Mal Sangham Lal* v. *Commissioner of Income Tax, Punjab*) and the learned Judges (Young, C.J., Coldstream, Monroe, Skemp, Bhide, Currie and Abdul Rashid, JJ.) have unanimously overruled *Chunnamal's Case* and followed the decision of the Calcutta High Court in *Krishna Lal Seal In re*. We may now take it to be settled law that in estimating the sum for which a property might reasonably be expected to let from year to year for the purpose of fixing its annual value, the amount paid by the tenant on account of municipal tax should be included, that is to say, should be treated as part of the rent payable by the tenant to the landlord. It must, however, be noted, as their Lordships have taken care to observe in this case, that the amount of rent payable by the tenant to the landlord is only *prima facie* evidence of the annual value and a consideration of the rents paid for similar and similarly situated properties in the locality may show the annual value in any particular case to be less or more than the rent actually paid.

Imposition of Penalty in Best Judgment Assessment Cases.

In *Benarsi Das* v. *Commissioner of Income Tax, Punjab & N.W.F.P.* (reported at page 217 of the current volume) certain important points relating to the imposition of penalty in best judgment assessment cases are discussed. Under Section 28 (1) of the Income Tax Act if the Income tax Officer, the Assistant Commissioner, or the Commissioner in the course of any proceedings under the Act, is satisfied that the assessee has concealed the particulars of his income he may impose a penalty. In *Benarsi*

Das's case there was a best judgment assessment and after rejecting an appeal therefrom on the ground that no appeal lay, the Assistant Commissioner imposed a penalty. The High Court held that, as no appeal lay and the appeal to the Assistant Commissioner was rejected on this ground, the Assistant Commissioner had thereafter no power to impose a penalty. The High Court further held that the Commissioner also cannot himself impose a penalty in further proceedings taken by the assessee under Section 32 or when an application was preferred to the Commissioner under Section 66 (2) of the Act praying that he may refer to the High Court the question of the validity of the imposition of the penalty by the Assistant Commissioner. It would thus appear that penalty can be levied in best judgment assessment cases only by the Income Tax Officer who makes the assessment.

It will be noted that in *Benarsi Das's Case* proceedings for imposition of penalty were started after the Assistant Commissioner had rejected the appeal. Has the Assistant Commissioner power to take proceedings for imposition of penalty before disposing of the case? We think the Assistant Commissioner would have no power to impose penalty even before disposing of the appeal, as under the Income Tax Act no appeal lies from an order of assessment made under Section 23 (4) and an appeal preferred against such an assessment cannot be regarded as ' a proceeding under the Act ' within the meaning of Section 28 (1).

Sir David Yule's Case

The Law Journal of England contains the following interesting note on *Sir David Yule's case* recently reported by us.

" All good subjects at home and overseas can scarce forbear to cheer when the Income Tax Commissioners suffer a reverse in the Law Courts; and no tears were shed when the Judicial Committee (Lords Thankerton, Russell of Killowen, Maugham, Sir Sidney Rowlatt and Sir Shadi Lal) upheld the judgment of the High Court of Calcutta in the case known as the *Income Tax Commissioner, Bengal* v. *Mercantile Bank of India Ltd.*, and others. The question arose in connection with the vast estate left by the late Sir David Yule, of India. The estate included holdings of shares in 30 companies.

The brief story as told by the High Court, was as follows. All the companies had very large accumulation of undistributed profits. . . . The trustee had to meet very heavy outgoings for duties both in the United Kingdom and in India in relation to the estate of the deceased, and it was to provide funds for such duties that a scheme was devised whereby accumulated profits would come into their hands and be available for the purpose of meeting such charges without, it was hoped, their rendering themselves liable to assessment to income tax in respect of such monies as by such means reached them. . . . The proposal was to capitalise the company's reserves and make a distribution to the shareholders in the form of debentures on redemption of which the funds required would be available.

The distribution and redemption duly occurred: and the Income Tax Commissioner asked whether the transaction represented income, profits or gains, etc., liable to income tax? The answer of the High Court of Calcutta and of the Judicial Committee was in the negative. The sum was not 'income' but 'capital'."

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Re-assessment : Scope of Sec. 34.

Upon the vexed question when income can be said to have 'escaped assessment' and can be re-assessed under sec. 34 of the Income tax Act, there are two recent judgments which deserve special notice. The first is a judgment of the Rangoon High Court reported at p. 209 of the *Income tax, Reports*, *Commissioner of Income tax Burma* v. *Dey Brothers*, and in this case the Chief Justice of the Rangoon High Court (SIR ARTHUR PAGE) has, with his usual ability and clearness of exposition discussed the scope of section 34. His Lordship's decision in *U Lu Nyo's* case (1933-1 I.T.R. 373)—that income in respect of which a final and conclusive assessment has been made by an income tax officer, cannot be subjected to a revised assessment by his successor merely because there is reason to think that the previous estimate of the income was too low—and the statement of the law made by his Lordship in that case have been emphatically re-affirmed, in spite of the fact that that case was dissented from by the Bombay High Court in *G. V. Manohar's* case (1935, 3 I.T.R. 438). With regard to the dissent of the Bombay High Court, the learned Chief Justice said :

'Further, I am of opinion that the animadversions passed by the Bombay High Court in *Commissioner of Income tax, Bombay* v. *G. V. Manohar* upon certain observations of a Bench of this High Court in *U Lu Nyo's case* were not justified. The learned Judges who decided *Commissioner of Income tax, Bombay* v. *G. V. Manohar* while agreeing with the actual decision in *U Lu Nyo's case* appear to have been under the impression that in *U Lu Nyo's case* this court had held that 'income from a particular source cannot be re-assessed under sec. 34'. With all due respect this court in *U Lu Nyo's case* did not and did not purport to lay down the law in that sense. In *U Lu Nyo's case* as in *Commissioner of Income tax Bombay* v. *G. V. Manohar* an income tax officer in a subsqeuent year of assessment, arriving at a different estimate of the income that had accrued in the

previous year from that at which the income tax officer in the previous year had arrived, proceeded to re-assess under sec. 34 the difference between the amount of the two estimates as being income that had escaped assessment in the previous year. That we held to be an attempt by one income tax officer to go behind and revise the assessment made by the income tax officer in the previous year merely because he disagreed with his predecessor's estimate of the amount of the assessable income. In that connection the court laid down that the Income tax officer had no jurisdiction to revise the assessment for the previous year which was completed and had became final'. We respectfully adhere to what was said in *U Lu Nyo's case* for in our opinion income in respect of which a final and conclusive assessment has been made cannot be subjected to re-assessment, except when the assessment has been made at too low a rate, either under sec. 34 or any other section of the Act.

In this case the income for the year 1930-31 was at first assessed at 14 per cent. of the sales at Rs. 8,267. Subsequently on the ground that the accounts for the year 1932-33 and 1933-34 showed 24 per cent. and 20·8 per cent. profits respectively on a smaller turnover, the income for 1930-31 was re-assessed at Rs. 68,267. It was held, applying the principle of *U Lu Nyo's case* that the re-assessment under sec. 34 was illegal and that the second assessment was not based on facts but on surmises and hypotheses for which there was no sound foundation and could not be sustained.

It may be noted that in commenting upon the Bombay case we had also stated that the Bombay High Court had not properly interpreted *U Lu Nyo's case* and that the dissent was unjustified (*vide* 1935 I. T. R. *Notes and Comments* p. 77.) We are glad to find that Rangoon High Court has re-affirmed *U Lu Nyo's case.*

The second case to which reference may be made is the decision of the Lahore High Court in *Nawal Kishore Khariati Lal* v. *Commissioner of Income tax, Punjab* reported at. p. 287 *infra.* The line which demarks this case from the case of *Dey Brothers* is a narrow one and it may perhaps be difficult to reconcile this case with *Dey Brothers' case* but for the fact that in *Nawal Kishore Khariati Lal's case*, the Commissioner found

from a comparison of the profits of earlier years that all the sales had not been truly entered in the account books on the basis of which the first assessment was made. The High Court held under these circumstances that the amount representing the profits on the sales which were not shown in the accounts had 'escaped assessment' and the Commissioner could not re-assess them under sec. 33 in the exercise of his revisional powers after the expiry of the period of one year prescribed for taking proceedings under sec. 34.

Registration of Hindu Undivided Family As Firms : Secs. 25 A and 26 A.

The decision of the Patna High Court in *Lachiram Baldeodas* v. *Commissioner of Income tax, Bihar and Orissa* (reported at p. 279) throws much light on certain questions which an income tax officer may have to decide when an application is made to him under sec. 26A for registration of a Hindu undivided family as a firm. Registration as a firm has certain advantages and instances where the members of a family produce a partnership deed and claim that they should be registered as a firm and be taxed as a registered firm and not as an undivided family are of common occurrence. The theory that there can be division of a family by unilateral declaration without an actual partition of the family property has given rise to some difficulties in ayplying sec. 26-A. WORT, ACTG., C. J., has laid down in this case that income tax authorities are not concerned with the notional separation in status in the eye of the law. In his Lordship's opinion, under sec. 25 A of the Income tax Act, the Income tax officer does not enquire into a question of separation or disruption of the family notional or otherwise; he has to enquire into the question of *whether the joint family property has in fact been divided.* And DHAVLE J., said : "Some of the argument before us has proceeded on the footing of what is called the notional separation of a Hindu joint family which sometimes gave rise to very difficult questions of law ; and the legislature has got over the difficulty by enacting specially in Sec. 25 A of the Act that what the income tax authorities have to proceed upon is whether 'the joint family property has been partitioned amongst the various members or groups of members

in definite portions". That is a concrete question of fact which it is fairly easy to investigate.

His Lordship has further held in this case that where there is no evidence to show that the family property has in fact been divided and it is not suggested that a partnership exists alongside the joint family firm an income tax officer would be justified in coming to the conclusion that the partnership alleged to exist between the members of the family is not genuine and in declining to assess the members of the family as a firm instead of as a Hindu undivided family.

Overdrafts on Security of Fixed Deposits.

The decision of the Lahore High Court in *Macnabb's case* (reported at p. 306 below) reveals one of the disadvantages of getting overdrafts from banks on the security of fixed deposits, especially to persons who do not carry on business. An assessee can claim a deduction of interest paid only in respect of capital borrowed for purposes of a business. Consequently, if a person who does not carry on business borrows money on the security of a fixed deposit made by him, he will have to pay income tax on the whole of the interest credited to him by the bank in respect of the fixed deposit. He will not be permitted to deduct the interest paid by him to the bank on the overdraft taken by him from the interert accruing due to him on the fixed deposit. Mr. Macnabb had a fixed deposit to the extent of Rs. 74,000 in a bank. He borrowed Rs. 66,600 from the bank for purchasing some shares as the fixed deposits had not matured. It was held that he was not entitled to have the interest paid by him to the bank on the overdraft deducted from the interest received by him on the fixed deposits.

We would invite the attention of Banks to this undesirable situation and think that if rules as to overdrafts on the security of fixed deposits are framed or agreements are entered into in such a way as to entitle the customers to get interest only in respect of the amount by which the fixed deposit exceeds the overdrafts, a method can be found out to save customers from being unnecessarily subjected to income tax.

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Jurisdiction of Civil Courts Over Income Tax Authorities.

The question when the ordinary civil courts can interfere and set aside acts of statutory authorities is a very difficult one and though it has been laid down in several cases as a general proposition of law that the civil courts can interfere if the authorities have acted ultra vires and that they cannot interfere if the authorities have merely acted illegally or wrongly, the application of this principle to the particular facts of a case is beset with difficulty. The line which separates ultra vires acts from acts which are illegal or wrong is somewhat narrow. Further, when the jurisdiction of the authorities depends on the existence of certain facts and the authorities have found these facts wrongly, the question arises whether these findings are also final though wrong, so as to preclude the civil courts from interfering. The decisions are to the effect that if the statute creating them has also invested them with the jurisdiction to determine the facts upon which their jurisdiction to act depends, their decision will be final even though their finding as to the existence of the facts which give them jurisdiction turns out to be wrong. These principles are discussed with particular reference to the acts of income tax authorities in an elaborate judgment by Varadachariar and Stodart, JJ., of the Madras High Court in a recent case decided on May 1, 1936, and reported at p. 341 below.

MEYYAPPA CHETTIAR'S CASE.

The exact question that had to be decided in the case was whether the civil courts have power to entertain a suit for a declaration that the plaintiff was not liable to be assessed to income tax as he was not residing in British India and for recovery of the tax levied from him. The Income tax authorities had found that he was a resident of British India and not of French territory as alleged by him, and had accordingly assessed him under the Indian

Income Tax Act. The High Court held that as the assessing authorities had jurisdiction to decide whether he was residing in British India and as they had decided after due enquiry that he was a resident of British India, their assessment cannot be questioned in the civil court. A brief reference to the earlier decisions will show that this judgment goes much further than those decisions and considerably narrows the powers of the civil courts.

Earlier Decisions.

In *Haji Rahmatulla Haji Pir Mahomed* v. *Secretary of State for India*, (92 I.C. 351), where the ground of denial of liability was that the profits did not accrue or arise in British India, it was held that the civil Courts had authority to interfere. In *In re Ramjidas Mahaliram* (62 Cal. 1011; 1936 I.T.R. 25) it was held that it is not for the Income tax Officer to decide whether the state of facts contemplated by sec. 34 exists and if he reopens the assessment without their existence he is acting without jurisdiction, and the civil courts could interfere. In *Rajah of Ramnad* v. *Secretary of State* (52 Mad. 17) it was laid down that where a certain income is outside the scope of the Act, such as agricultural income or income not earned in or brought into British India any assessment in respect of such income would be outside the scope of the Act and a civil suit to recover it would not be barred. Similarly, in *Dayaram Ramdas* v. *Secretary of State for India* (78 I.C. 940) it was observed that if the income tax authorities had levied assessment on the classes of income exempted by the Act they would have overstepped the limits of their jurisdiction and the assessment would not have been under the Act. The learned Judges of the Madras High Court have got over all these decisions and opinions and held that even where the assessee claims to be a non-resident the civil Courts have no power to interfere. Where the assessment is impeached on the ground that the assessee did not reside within British India and was consequently beyond the jurisdiction of the Income tax Officer—indeed beyond the limits where the Income tax Act applies—the assessee has a case much stronger than the earlier cases just referred to.

On Principle

Upon principle also the decision seems to go very far; for assessment of a person who is not a resident of India seems clearly

to raise a question of jurisdiction and stands on a different footing from assessment of one who merely contends that under some provision of the Income Tax Act he is not chargeable. We also find nothing in the Income Tax Act to warrant the view that the legislature has invested the income tax authorities with the jurisdiction to decide finally whether a person is a resident of British India or not. The reference to Secs. 42 and 43 is not much in point as under those sections it is the agent of the foreigner, who resides in India who is taxed. The Act says 'No suit can be brought to set aside or modify an assessment made under the Act'. The fact that the legislature has not used the expression 'an assessment *made or purporting to have been made* under this Act'—an expression with which it is quite familiar—also has some significance. In any event the section does not preclude the civil courts from granting a declaration of the status of the assessee and his non-liability to be taxed, at least so as to protect him from being assessed similarly in future, even assuming an assessment actually made cannot be set aside or the amount paid refunded.

Non-Residents.

The Judgment of the Judicial Committee in the *Bombay Trust Corporation case* (reported below at pp. 328 to 340, deserves the careful attention of foreign companies and other non-residents. Sections 42 and 43 of the Indian Income Tax Act empower the income-tax authorities of India to tax foreigners who derive profit through a business connection in India. The Hong Kong Trust Corporation had a business connection with the Bombay Trust Corporation and it was held by the Judicial Committee in the year 1930 that in respect of interest paid by the Bombay Co., it can be treated as an agent of the Hong Kong Co., and that it can be assessed to income-tax as such. The Bombay Co., was being thus assessed till 1926. During the latter part of the year 1926 in order to avoid being taxed in this way the Hong Kong Corporation and the Bombay Corporation agreed that all fixed deposits should be converted into call loans and that the entire loan should be paid back to the Hong Kong Co., through their common banker. The Bombay Company thereafter took loans from this bank and paid interest to the bank. The income-tax authorities again taxed the Bombay Company on the interest paid in 1927 on the ground that all the three companies including the banking company were under the control of the same persons and working in concert and the interest paid to the bank really represented the

profits of the Hong Kong Company. The Judicial Committee held that there was no material upon which the income tax authorities could come to such a finding and that the assessment was illegal. The entries in the accounts clearly showed that the loans were taken from a third party, a banking company, and the income tax authorities were not entitled in the absence of evidence, to treat the loan by the banking company as a loan by the Hong Kong Company.

Sir George Rankin in delivering the judgment observed:

'However sceptical the attitude which the income tax authorities many think fit to adopt towards the declarations offered and the entries made in the Bombay Company's books, it is necessary, if the assessment is to be supported, that there shall be some evidence to show that in 1927 the loan from the Hong Kong Co., continued and that interest accrued or arose to that company thereon.'

As his Lordship has pointed out later on, the question at issue has to be decided according to the legal rights resulting to the parties from what they in fact did and agreed to do. If the lender really accepts a credit in the books of a third party in discharge of the loan and if the borrower really intends to become liable to that third party, the borrower succeeds in changing his financier. Where the only evidence is to that effect it is not, in the absence of any positive evidence, sufficient to entitle the income tax authorities to hold that the quondam lender still continued to be the lender and to receive the interest.

Foreign companies and non-residents who find themselves in the predicament of the Bombay Trust Corporation would be well advised in following the procedure adopted by the assessees in the present case.

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NOTES AND COMMENTS.

Commissioner's Power To Demand Security Before Refunding Tax Pending Appeal to Privy Council.

We had adverted to the main point decided by the Judicial Committee in *Commissioner of Income Tax, Bombay Presidency* v. *The Bombay Trust Corporation Ltd*, (1936, 4 I. T. R. 323) in our September issue. The judgment contains some further pronouncements on the powers of the High Courts and Income Tax Commissioners which require notice. Where an assessment is declared to be illegal by the High Court on a reference, is the Commissioner entitled, before refunding the income tax to the assessee, to demand security from the assessee or any third person for the payment of the tax in case the tax is levied again or an appeal which the Commissioner intends to prefer to the Privy Council proves successful. Upon this question the Bombay High Court had held that the Commissioner had no such power and the Judicial Committee have upheld this view in these words: "Their Lordships cannot but agree, however, with the comments made by the learned Chief Justice upon the Commissioner's order imposing as a condition of refund that Messrs. E. D. Sassoon & Co. Ltd. should undertake to be responsible for paying back the amount in case an assessment were levied again or the matter was taken on appeal to the Privy Council".

Power of High Court to Direct Commissioner to Refund Tax Illegally Levied.

The Judicial Committee appear to be of the opinion that where the High Court has found in a case referred to it under Section 66 of the Income Tax Act that the assessment in question is illegal, it has no power under the Specific Relief Act to direct the Commissioner to refund the tax illegally levied, in view of the fact that a decision under Section 66 is only 'advisory' and in view of clause (*g*) of Section 45 of the Specific Relief Act which provides that nothing contained in Section 45 "shall be deemed

to authorise any High Court to make any order on any other servant of the Crown as such merely to enforce the satisfaction of a claim upon the Crown". The Judgment of the Judicial Committee is however not very clear, for, though it is stated in one place that 'the action taken by the High Court under the Specific Relief Act was however incorrect', we find later on a passage to the following effect: "Whether the Commissioner of Income Tax either generally or under Section 66 (5) of the Income Tax Act is in this position as regards the refund of tax paid under an invalid assessment is the question raised by Clause (*g*) of Section 45 of the Specific Relief Act. This their Lordships do not find it necessary in the present case to decide."

Commissioner's Power to Order Re-enquiry After Adverse Decision of High Court.

There are also some observations in the judgment of the Judicial Committee in the abovesaid case, namely, *Commissioner of Income Tax, Bombay* v. *The Bombay Trust Corporation* (1936, 4 I. T. R. 323) regarding the power of the Commissioner to make a further enquiry after an adverse decision of the High Court in a case referred by him (vide pp. 337-338). Under Section 66 the Commissioner has to state all the facts and his findings thereon in a reference, and investing the Commissioner with power to burke the decision of the High Court and start the entire proceedings afresh by making further enquiries when the decision of the High Court goes against him may render the whole proceedings before the High Court futile; but this passage in the judgment of the Judicial Committee is also somewhat obscure and we have to await a clearer pronouncement on the subject. Though the decision of the High Court in a reference under Sec. 66 of the Act may be merely advisory, the advice given is intended to be followed and not 'flouted or ignored' as the learned Chief Justice of the Bombay High Court has said; and the power of the Commissioner under the Income Tax Act to direct a further enquiry is not intended to enable the Commissioner to override or ignore the opinion of the High Court.

Bad Debts : Confused State of the Law.

The judgments of the Lahore High Court in the cases of *Harnand Rai Harbhagat Rai* v. *Commissioner of Income Tax*,

Punjab & N. W. F. P., *Commissioner of Income Tax, Punjab* v. *Hukum Chand Jagadhar Mal* and *Som Chand Maluk Chand* v. *Commissioner of Income Tax, Punjab* (reported below at pages 336, 380 and 382 respectively) show that the law relating to bad debts is in a very unsettled state. In these cases we find the Income Tax Officer, Assistant Commissioner, Commissioner and the High Court coming to diametrically opposite conclusions on the question when a debt becomes bad on the very same set of facts.

In the first case the Income Tax Officer held that a debt claimed as a bad debt in 1931-32 had not yet become bad in that year. The Commissioner held that it had become bad in 1928 and the High Court held that it could not have become bad till 1931-32.

In the second case the Income Tax Officer held that the debt had become bad in 1929. On appeal the Assistant Commissioner held that the debt had not become bad even in 1932-33. The Commissioner agreed with the Income Tax Officer; but the High Court held that the debt had not become bad in 1929 and that whether it became bad in 1932-33 or later was a question of fact to be decided by the Income tax authorities.

In the third case the Income Tax Officer held that the debt in question had not become bad in 1932-33. The Assistant Commissioner held that the debt had become bad in 1930. The Commissioner agreed with the Assistant Commissioner; but the High Court held that the Commissioner's opinion was not based on any evidence or reasoning and that the debt had not become bad in 1930.

If there can be so much divergence of opinion on the question when a debt can be said to have become bad the position of assessees is quite insecure.

All this confusion is, in our opinion, due to a fundamental error in approaching the question. As we have pointed out in our Notes and Comments in Volume III of the *Income Tax Reports* page 56 the question as to when a debt becomes bad is not a fact which can be proved by any evidence like other tangible facts. No one can specify the exact point of time when a debt becomes bad. The financial stability of a debtor often changes gradually and imperceptibly. When a debt becomes bad is really *a matter of opinion and the opinion of the creditor must be respec-*

ted and acted upon by the income tax authorities and the Courts unless it is proved to be capricious or *mala fide.* It is a matter for regret that the Judicial Committee did not lay sufficient emphasis on this aspect of the question in *Sir S. M. Chitnavis' Case* but simply laid down that "whether a debt is a bad debt and, if so, at what point of time it became a bad debt, are questions of fact to be determined, in case of dispute, by the appropriate tribunal upon a consideration of all relevant and admissible evidence" We have adverted to this matter in detail once and do not wish to dwell upon it further. We may, however, point out to our readers that the judgment of the Lahore High Court in the third case referred to above, namely, *Som Chand Maluk Chand's case* is an authority for the position that a creditor is not bound to strike off a bad debt as a debt as soon as he finds that his debtor is in difficulties. SIR JAMES ADDISON and ABDUL RASHID, JJ., have observed in this case that "It does not follow that because a firm is in difficulties it will never recover and that all debts due by it should immediately be struck off as bad debts".

Liability of Executors.

The Judgment of the Privy Council in the case of *The Trustees of The Sir Currimbhoy Ebrahim Baronetcy Trust* [2 I. T. R. 148] establishes that trustees are liable to pay income tax on the income of the trust property. Similarly executors are liable for income tax in respect of the income which finds its way into their hands in their capacity as executors. *A. H. Forbes* v. *Secretary of State for India* (I. L. R. 42 Cal. 151) and the recent case of *P. C. Mallick and D. C. Aich In re* (reported at page 369) are instances where executors have been so held liable. Two other important points relating to assessment of executors have now been decided in the case of *P. C. Mallick and D. C. Aich, In re.*

Cost of Obtaining Probate.

Where the testator has provided that the cost of obtaining probate is to be met by the executors out of the income of the estate, are the executors entitled to claim that such cost should be deducted in computing their chargeable income? In other words, is the expenditure so incurred an allocation of the revenue of the

estate before it becomes income in the hands of the executors or is it an application by the executors of a part of the income in their hands in a particular way. The Calcutta High Court has held in this case that it is not case of allocation of revenue before it becomes income but only application of the income which has come into the executors' hands, and that consequently such expenditure cannot be deducted in computing the chargeable income of the executors.

Amounts paid Out of Income For Performance of Testator's Addya Sradh.

The other question which has been dealt with in this case is whether, when there is a provision in the will directing the executors to pay a certain amount for defraying the expenses of the testator's *addya sradh* (a religious ceremony in connection with the death of the testator) to the person who is entitled to perform the same under the Hindu Law, the executors are entitled to claim that the entire amount so directed to be paid or the portion of the amount which is actually paid during the year of account in accordance with this direction, must be excluded from the chargeable income.

Their Lordships have answered the above question also in the negative, that is to say, they are of opinion that neither the entire amount directed to be paid nor the actual amount so paid can be deducted. Such expenditure is also not an allocation of the revenue before it becomes income in the executors' hands but an application of the income in a particular way.

This principle is, we presume, not confined to the particular kind of expenses considered in this case but will also apply to other directions contained in a will for application of the income of the estate in a particular way. In such cases, merely because a provision is made in the will itself, it cannot be held that the chargeable income of the executors is only what remains after the directions of the testator are carried out. As their Lordships have observed in this case, *Bejoy Singh Dudhuria's Case* in which it was held that an amount payable to the assessee's step-mother for maintenance under the directions of his father's will could not be regarded as income in the assessees' hands is distinguishable from cases of this nature.

Death of Partner Before Assessment of Firm : Right of Partners' Heirs to Claim Refund Under Section 48 (2).

The decision of the Judicial Commissioners' Court of Sind in *Zenab Kaderbhoy* v. *Secretary of State for India* (reported below at page 389) in which RUPCHAND BILARAM & HAVELIWALA, Additional Judicial Commissioners, have confirmed on appeal the decision reported in 22 S.L.R. 426 raises a question of some importance to businessmen. Where a registered firm has been assessed on its profits and the rate of income tax payable on the income of the individual partners is less than the rate at which the profits of the firm were assessed, Section 48 (2) of the Indian Income Tax Act entitles the members of the firm to a refund on their shares of the profits calculated at the difference between the two rates. If the total income of the member in the previous year was below the minimum chargeable, then also the section (as amended in 1933) entitles the member to a refund of the income tax which has been levied on his share of the profits. Where a partner dies before the year of assessment, is his legal representative entitled to claim a refund on the share of the profits of the deceased partner which had devolved on him? In the above-mentioned case it has been held that Section 48 (2) applies only to a person who has been assessed and does not apply to a person who was dead before the assessment on his income was made and that in a case of this nature the partner's legal representatives are not entitled to a refund under Section 48 (2). In this case there was no doubt the fact that the firm itself was registered only after the death of the partner whose legal representative was claiming the refund but the judgment seems to proceed on a wider ground. If the decision is right, the position of the heirs of a deceased partner is a little anomalous and the legislature must set matters right. There is no reason why if the living partners can claim a refund, the heirs of a deceased partner cannot. The death of a partner should not be made a ground for not giving a refund to which he would have been entitled if he had been alive.

No doubt there is a new section, sec. 48 A, Sub-section (1) which confers a general power to make refunds but it is doubtful whether the wording of that section would cover a case like this.

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NOTES & COMMENTS

ASSESSMENT OF CO-OWNERS AS AN ASSOCIATION OF INDIVIDUALS.

THE CASE OF B. N. ELIAS and others, *In re.*

Our readers may remember the case of *B. N. Elias and others, in re* (1935 I. T. R. 408) and our comments on that decision at page 81 of the Notes and Comments in the same volume. It was held in that case that four persons who had purchased a property consisting of buildings in certain definite shares as tenants in common constituted an association of individuals and could be assessed as such. We expressed some doubt about the correctness of that decision and observed:

"We think a distinction must be made between co-owners who enjoy property as tenants in common and an association of individuals owning property. The expression 'association of individuals' is intended to apply to combinations such as clubs, societies and other institutions and is not applicable to co-owners of immoveable property holding definite shares therein even though they might have purchased the property under the same sale deed and appointed an agent by the same power of attorney."

VIEW OF THE ALLAHABAD HIGH COURT.

The decision of the Allahabad High Court in a recent case reported at p. 412 below (*Mohammad Aslam* v. *Commissioner of Income Tax, U. P.*) has removed the misconceptions likely to arise from the decision of the Calcutta High Court in *In re B. N. Elias*. The learned judges of the Allahabad High Court have held in this case that the expression 'association of individuals' in Section 3 of the Income Tax Act is not wide enough to cover the case of a number of persons having specified but undivided shares in property which produces income. Their Lordships say that the expression is *ejusdem generis* with the word immediately preceding, *viz.*, 'firm' and that before there can be an associ-

ation of individuals within the meaning of the section it must first be shown that the association has at least some of the attributes of a firm or partnership though not in the strictly legal sense of the term. Their Lordships have further held that the appointment by a body of co-owners of a common collecting agent will not convert such a body into an association of individuals. But they have expressly refrained from giving an opinion as to what the position would be if the co-owners of an income-producing property appoint one or more persons, whether from among themselves or from outside, to perform all the functions of a common scheme of management. Even in such a case we are clearly of opinion that the income of co-owners who hold definite shares in specific immoveable property cannot be assessed as the income of an association of individuals.

The True Test.

Though the learned Judges of the Allahabad High Court have rightly laid down that a body of mere co-owners having undivided but definite shares cannot be treated as an association of individuals, the reasoning on which they have based their decision and their definition of the attributes of an association are open to criticism. The absence of a comma after 'firm' does not lead to an inference that the expression 'other association of individuals' is bracketed with 'firm'. When we say 'A, B and C,' the absence of a comma before 'and' does not lead to any inference that there is a closer connection between C and B, than between C and A. If any such closer connection is intended we must put an 'and' before B also. The expression is, we think, *ejusdem generis* not with firm alone, but with the previous expressions, Hindu undivided family, company and firm.

In Section 3 of the Income Tax Act the legislature is enumerating the different classes of assessable units, that is, the different kinds of legal entities in which the ownership of income may be vested. Under the section income of individuals, of Hindu undivided families, of companies, of firms and of other associations of individuals are liable to be taxed. When there are a number of persons interested in an income what we have to determine is whether it is the income of the individuals or the income of an association composed of those individuals. The mere fact that those several persons have a common under-

standing or have joined together for some common purpose will not convert income which belongs to them in defined shares into income of an association. In order that such income may become the income of an association the combination must result in the formation of an association or body which can own the income, and income must in the eye of the law belong to the association as distinct from its members. So long as the act of joining or combination does not result in such an association, the income remains the income of the individuals and has to be assessed as such. This distinction becomes clear when we consider the nature of clubs, trade unions, societies, trustees, castes and other similar bodies. In the case of such a body the income is truly the income of an association of individuals and not of the individuals who form it. The members have no right to any definite share in the income. The income belongs to the association and can be disposed of only in accordance with the wishes of the association, that is, of the majority of the members who constitute the association.

The true test therefore, is not whether the individuals concerned have joined together for any common purpose, but whether, in the plain words of Sec. 3 of the Income Tax Act, the income in question is in the eye of the law the income of the individuals or the income of an association of which they are the members.

Assessee's Right to Change his Method of Accounting.

The High Court of Bombay has in a recent case reported at page 420 below, *Sarup Chand* v. *Commissioner of Income Tax, Bombay Presidency*, made some clear pronouncements on the question whether an assessee is entitled to change the method of accounting regularly adopted by him. The Commissioner of Income Tax, Bombay, was of opinion that a method once regularly adopted cannot be changed by an assessee. Referring to this view the learned Chief Justice (Sir J.W.F. BEAUMONT) said :

"I desire to say that I am not altogether in agreement with the reasoning on which the learned Income Tax Commissioner bases his order . . . . It seems to me impossible to contend that an assessee is never at liberty to alter the regular method which he has once employed."

And RANGNEKAR, J., said:

"I do not agree with the Commissioner that it is not open to a person to change a method which he has regularly employed for some years at any period in a particular year. There is nothing in the Section (Sec. 13) or the Act to prevent an assessee from changing his method."

The important thing to be noted in this connexion is, as the learned Chief Justice has said, what he (the assessee) must alter however is his regular method, that is to say, he must abandon what, up to that time has been his regular method, and start a new regular method and not merely a new method for a casual period.' He cannot change his method from year to year as suits him best. The reference in Section 13 to the regular method of keeping account precludes any practice of that sort.

The question whether the assessee has adopted a new regular method is a question of fact for the Commissioner to decide and on which the Commissioner cannot be required to make a reference, but if an assessee has in fact changed his method for a new regular method the Commissioner is, as the learned Judges have said, bound to recognise the new method.

The present unsatisfactory state of the law as to bad debts and as to when interest which has accrued but has not been actually received can be assessed, makes the mercantile system of accounting a very risky one, especially to money lenders. Several pitfalls can be avoided if the cash systen is adopted and those who carry on money lending business would, we think, be well advised in changing the mercantile system to the cash system. As we had occasion to observe on a former occasion it is not very prudent to pay income tax in advance on amounts which we have not actually received and then claim such amounts subsequently as bad debts.

Reference: Assessee's Right to Return of the Deposit of Rupees One Hundred As Costs.

Doubts have been entertained in some quarters as to whether the deposit of Rs. 100 which an assessee has to make, under Section 66 (2) of the Indian Income Tax Act, along with an application for a reference to the High Court, forms part of the costs of the reference. The practice of the High Courts of Madras, Allahabad, Patna and Lahore has been to treat this

deposit as part of the assessee 's costs. The Rangoon High Court also approved of this pactice in *Commissioner of Income Tax, Burma* v. *J. I. Milne* (1934 I.T.R. 25). In the Bombay High Court the practice seems to have been otherwise but in a recent case reported at p. 417 below (*Commissioner of Income Tax, Bombay* v. *Gopal Vaijnath Manohar*) the question was raised and the learned judges have held that the practice prevailing in the other High Courts is correct. Their Lordships have held that the deposit forms part of the assessee's costs of the reference and that an order directing the Commissioner to pay the assessee's costs in a reference entitles the assessee to a return of the deposit made by him. Their Lordships also point out that the correct procedure for the High Courts is not to order the Commissioner to refund the deposit to the assessee but to treat it as part of the costs. They have further stated that in cases in which the assessee is ordered to pay costs the Court can if it considers that credit should be given to the assessee for the fee, give the Commissioner his costs less Rupees one hundred. The last point is one which assessees who may not succeed in a reference may remember with advantage.

Assessment of Chamber of Commerce.

A very important decision relating to the assessment of the income of Chambers of Commerce and similar associations which partake of the character of mutual concerns has been pronounced by the Allahabad High Court in *The Chamber of Commerce, Hapur* v. *Commissioner of Income Tax, U.P.*, reported below at page 397. Though such associations are mostly mutual concerns they usually widen their activities and earn an appreciable amount of income. It is settled law that so far as they are purely mutual concerns their income is exempt from income tax: *Styles' Case* (14 A.C. 381), but complications arise when they engage in doing business with their own members or with outsiders, and it is also difficult to decide whether their activities are purely of a mutual nature or amount to business or trade. If such associations engage in business and earn profits therefrom there is no reason why the profits so raised should not be assessed. In the present case the association was mainly intended to promote the interests of the corn merchants in a certain locality and to facilitate business dealings bet-

ween the members and outsiders. Its income was derived from two sources: (1) admission fees and annual subscriptions of the members (2) registration fee for grain pits and commission on every purchase and sale on forward delivery contract entered into between the members or between a member and an outsider or between outsiders. The income tax authorities exempted the admission fees and subscriptions from tax but held that the commission and registration fees were assessable. The Commissioner held that this income was not income from business but it was nevertheless assessable as income from services rendered by the association to the members. On a reference to the High Court it was held that if the income could be assessed at all it could be assessed only as income from business and, as the Commissioner had conceded that it was not income from business, it was not assessable. The learned Judges however expressly state that they do not decide whether the income was derived from business. The case has proceeded entirely on the admissions made by the Commissioner and there was no necessity for the Judges to consider the important question whether income derived in this way is income from business and liable to be assessed as such. For a definite answer on this question we have to await future decisions relating to assessment of similar associations. The Income Tax Authorities will not, of course, concede in future that such income is not income from business.

Chamber of Commerce, Whether a Charitable Institution.

Their Lordships have however expressed clear opinions on two points relating to such associations, *viz.*, first, that the mere fact that an association of this kind has been registered as a limited company under Section 26 of the Indian Companies Act (which provides for the registration of associations not formed for profits as limited liability companies) is not sufficient to exempt its income from assessment to income tax. The second point is that such institutions are not charitable institutions within the meaning of Section 4 (3) (ii) of the Indian Income Tax Act and are not exempt from assessment as such. Their Lordships say that before an institution can be held to be charitable there must be an element of altruism, that is to say, the beneficiaries must not be able to claim the benefit. Further, they doubt whether

the object of such an association is one of 'general utility' as contemplated by Sec. 4 (3) (ii) of the Indian Income Tax Act.

Commissioner Stating Himself out of Court.

Now and then we come across cases where the Commissioner 'states an assessee out of Court.' The case of the Hapur Chamber of Commerce is a case—a very rare one—where a Commissioner states *himself* out of Court. As the learned Judges of the High Court have held, the income sought to be assessed by the Commissioner could be assessed, if at all, only as income from business, but the Commissioner had agreed with the assessee and conceded that the income was not assessable as income from business.

The Mylapore Permanent Fund Case Commented upon.

There are a large number of mutual benefit societies especially in South India which advance loans to their subscribers or shareholders and make large profits therefrom. In the *Mylapore Permanent Fund* Case (I.L.R. 47 M. 1) the Madras High Court applied the principle of *Styles' case* (14 A. C. 381) to such cases and held that the income of such societies derived from interest paid by the subscribers or shareholders on loans advanced to them is not liable to income tax. Though in several subsequent rulings of the same High Court this case has been followed, the income tax authorities have not yet been able to appreciate the soundness of this decision. It will be of some interest to Revenue authorities to know that this decision has been commented upon by the Allahabad High Court in the recent case cited above, *viz.*, *Chamber of Commerce, Hapur* v. *Commissioner of Income Tax, U.P.* After referring to the abovesaid decision of the Madras High Court, COLLISTER, J., who delivered the leading judgment in this case said:

"The question does not seem to have been considered whether a mutual concern can trade with its members and whether the payment and receipt of interest on loans advanced might not amount to a money-lending business between the association and its members."

Transfer of Government Securities: Liability of Transferee to pay Income Tax on Interest.

Where Government securities are transferred the parties usually calculate interest up to the date of transfer and the trans-

feree pays to transferor the value of the securities and of the interest which had become due up to the date of transfer. But the decisions are to the effect that income tax will be levied from the transferee not merely on the interest which accrued due after the date of transfer but also on the interest in respect of the period between the last previous due date up to the date of transfer, for, interest on securities does not accrue from day to day but only on the due dates and interest which is paid on a specific due date is the income of the person who is the owner of the securities on that date. This principle which was laid down in the English cases of *Wigmore* v. *Summerson & Sons* (9 Tax Cas. 577) and *Commissioners of Inland Revenue* v. *Oakley* (9 Tax Cas. 582) and applied in India in *Ranjit Prasad Singh* v. *Commissioner of Income Tax, Bihar & Orissa* (1930, I.L.R. 9 Pat. 194) has been re-affirmed very recently in a case which came up before the Lahore High Court and is reported at p. 297 of 1936 I.T.R. as *Haveli Shah Sardari Mal* v. *Commissioner of Income Tax, Punjab*. It is obvious that the vendee in such cases has to pay tax on an income which is not his but the vendor's but the proper remedy of the vendee is contained in the following observations made by their Lordships:

"The form the contract took and the terms in which it was expressed were matters between the assessees and the vendors, and the assessees might well have protected themselves by insisting that the amount of tax which would ultimately be payable by them under Sec. 8 should be deducted from the purchase money." But this protection alone may not be sufficient if the vendee is near the super-tax level.

The principle is thus expressed by ROWLATT, J., in *Wigmore's* case:

"The truth of the matter is that the seller does not receive interest while it is interest that is the subject matter of taxation. He receives the price of the expectancy of interest and that is not the subject of taxation."

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NOTES AND COMMENTS.

Agreements Allowing Managing Agents to Retain Share of Profits as Remuneration.

NRISINGHA CHANDRA NANDY'S CASE,

(1936 I. T. R. 428)

A question of great importance to businessmen has been decided by the Calcutta High Court in *Nrisingha Chandra Nandy In re* (reported below at pp. 428 *et seq.*) The decision reveals the dangers, from an income-tax point of view, of agreements between proprietors and managing agents allowing managing agents to retain a share of the profits of the business as their remuneration. The hardship which such agreements cause to the proprietors has evoked the following remarks from the learned Chief Justice (SIR HAROLD DERBYSHIRE) :—

"I must say that I have come to this conclusion with considerable reluctance, because it appears to me that the assessee is being assessed to tax upon a sum of money which he never received in full and which he was not entitled to receive in full. But such is the operation in my view of the income-tax law in this particular case. The assessee has unfortunately made an agreement for the division of the trading surplus of this concern as between himself and his managers without having regard to the incidence of income-tax as laid down by the law."

THE DECISION

The assessee who was the proprietor of a business entered into an agreement with certain other persons appointing the latter as managers for a period of five years, and authorising them to carry on and conduct the assessee's business. The managers were to pay the assessee 5 per cent. on the gross realisation and Rs. 1,000 per year and to retain the balance of

the profits of the business as their remuneration. The total profits of the business for a year amounted to Rs. 45,082. The assessee received Rs. 14,510 under the terms of the agreement, and the managers retained the balance, namely, Rs. 30,572. It was held that the assessee was bound to pay income-tax not only on Rs. 14,510 but on the entire profits of the business, namely, Rs. 45,082. The hardship is obvious.

The Ratio Decidendi.

The reasoning on which the judgment is based is this. Though the assessee had entrusted the entire management and executive control to the managing agents he was the person who 'carried on the business' within the meaning of Section 10 (1) of the Income Tax Act, and not the managing agents, and, as such he was the person liable to be assessed in respect of the profits of the business. He cannot claim a deduction of the sums retained by the agents for their services, as business expenditure, for, a payment out of profits and conditional on profits being earned cannot be described as a payment made to earn profits as laid down by the Judicial Committee in the *Pondicherry Railway Co.'s Case* (58 I.A. 239). Panckridge, J., is of opinion that Section 10 (1) of the Income Tax Act which occurs in Chapter III is not controlled by Section 3 which charges only the income, profits or gains of the assessee.

A Few Suggestions.

The question is obviously one of great difficulty but we think the following points can be advanced in favour of the proprietors when similar cases arise before the other High Courts :—

(1) The opinion of Panckridge J., that Chapter III of the Income Tax Act in which Section 10 (1) occurs is not controlled by Section 3 is open to doubt. Section 3 is the section which charges the income. Chapter III merely deals with the heads of income which are to be charged. Chapter III cannot extend the scope of Section 3 or impose liability in cases which do not come under Section 3.

(2) The liability to be assessed arises from receipt or accrual of income and not from ownership or proprietorship of business and the person liable to be assessed is the person to whom income accrues or who receives the income.

(3) Unless we come to the conclusion that in the case of such agreements the proprietor is, in the eye of the law, the person who receives the income and that the receipt by the managers is not in their own right but for the proprietors, the proprietor cannot be assessed. If the true view is as the learned Chief Justice has said 'that the assessee never received the income and was not entitled to receive it', the judgment cannot be supported.

(4) In the *Pondicherry Railway Co.'s Case* the assessees were admittedly entitled to receive the entire profits and did receive the entire profits. The Judicial Committee only held that subsequent payment by them out of the profits received by them cannot affect their liability to be taxed. This case is no authority for assessing a person who has not received the income and to whom the income has not accrued—who in fact is not even entitled to receive the income. Agreements which vest the right to receive the profits in another person giving the assessee only a right to receive a share of the profits from that person are not covered by *Pondicherry Railway Co.'s Case.*

(5) The crucial question in such cases seems to be whether the income in question has accrued to the assessee or has been received by him—in fact or in the eye of the law—and this point has not been considered in the Calcutta Case.

Necessity of Paying Attention to the Incidence of Income Tax in Framing Agreements.

The observations of the learned Chief Justice which we have quoted above show the necessity of paying attention to the incidence of income-tax as laid down by the law, in framing agreements relating to business. In ninety-nine cases out of hundred, by slightly changing the wording of the agreement or the legal relationship between the parties concerned, many pitfalls of income-tax law can be avoided. We need only refer to the recent case of the *Bombay Trust Corporation Ltd.*, [1936 I. T. R. 323] for a typical instance, whereby an intelligent, but for all practical purposes immaterial, alteration in the jural relationship between the parties, the assessees relieved themselves of a very heavy burden of income-tax. In drafting agreements involving large sums of money it is always advisable to consult specialists in income-tax law also.

RECENT HOUSE OF LORDS CASES.

Payments Out of Capital May be Income of Recipient.

The principle that a payment out of corpus may properly be assessable income in the hands of the recipient was applied by the House of Lords in a recent case, and, as similar questions are likely to arise in India also, the case is reported in the *Income Tax Reports*: See *Williamson* v. *Ough* (1936 I.T.R. Eng. Cas. 1). A testator directed his trustees under the will to make certain annual payments to a beneficiary out of the income and further provided that such payments should be made out of capital if there was no income. Trustees were also empowered to recoup payments made out of capital, from the income as and when the trustees should think proper. It was contended that the payments made out of capital were mere loans repayable by the recipient, but the House of Lords (The Lord Chancellor, Lord Blanesburgh, Lord Russel of Killowen, Lord Macmillan and Lord Roche) held that the payments made could not be regarded as loans made to the recipient to tide over the period when there was no income and that they were assessable to income-tax in the hands of the beneficiary. Lord Russel of Killowen said: "It is well-settled that a payment out of corpus may properly be assessable income in the hands of the recipient. A familiar instance is the case of an annuity charged on the income and corpus of an invested fund: all moneys raised out of corpus to provide the amount of the annuity will be assessable income. The present case presents a close analogy."

Sale of Property Stipulating for Annual Rent Charge.

Where a property is sold partly for cash and partly in consideration of a annual rent-charge what is the basis for calculating the profits made by the vendor? Is the right to receive the annual rent also to be taken into account and, if so, how is it to be valued? These questions are answered by the House of Lords in *John Emery & Sons* v. *Lord Advocate* [1936 I.T.R. Eng. Cas. 8]. Lord Atkin states the legal effect of such a transaction in these words:

"It is a case where people have sold in the course of business part of their stock for money plus money's worth, namely,

the equivalent of a marketable security. The position in respect of ground annuals appears to me to be precisely the same as though they had sold the land for money plus an annuity or plus a bond conditioned for the payment of these particular sums, or for debentures under which those sums were payable annually ; it could be put in a great many different ways. However you put it, the result is not that they exchange part of their stock for a different kind of stock, but that they dispose of the whole of their stock for money plus money's worth In these circumstances it seems to me on the plainest principles that the value of that marketable security has to be brought into account for the purpose of assessing the profits which they made in the particular years of trade."

Referring to the ground annuals LORD THANKERTON said: " It does seem to me that the proper view of that part of the transaction is that in effect the appellants agreed to leave part of the price as a real burden on the property to the extent of the well-known marketable value or thereabouts at the time."

To the argument that this could not be brought in until its value was realised by the vendors, as they could do, in the market, the noble Lord said ; " if part of the price paid for the land and the buildings consisted of money's worth, the marketable value of which assets is immediately ascertainable, I fail to see why that should not be brought into computation in the ordinary accounts of the trader for the purpose of bringing out the results of his year's trading."

CHARITABLE PURPOSES

Foxhound Societies : Whether Charitable Societies

In *Peterborough Royal Foxhound Show Society* v. *Inland Revenue Commissioners* [1936 I. T. R. Eng. Cas. 18] decided in the Kings Bench Division, a society whose object was to promote the interests of foxhound breeding claims exemption from income-tax on the ground that it was a charitable society, that is, a society established for charitable purposes only. It was urged on behalf of the society that its object was beneficial to the community and that consequently it fell within the fourth category of charitable trusts enumerated by LORD MACNAGHTEN

in *Pemsel's Case* (1891 A.C. 531). It was contended that fox-hunting is good for the community at large 'because it keeps money in the country and brings it into the country side, that it was good for the officers in the army and those who take part in it and that it makes for the well being of animals, which is for the benefit of the community.' LAWRENCE, J., repelled this contention saying: 'Though I am firmly convinced of the truth of these propositions of fact, I am unable to take the view that the appellant society is established for charitable purposes only."

Test of Charitable Society: Main though Indirect Purpose.

LAWRENCE, J., has made some valuable observations in this case which are of great help in determining whether a society is a charitable society or not. His Lordship says that the difficulty in this class of cases arises principally from the mixture of motives or purposes which appears to exist in the minds of the founders of such societies. A society may be established with an immediate direct but incidental motive or purpose which is not charitable for example, to promote the sports of a particular regiment but with an ultimate indirect but main purpose, which is charitable; and in that case it comes within the exemption." Applying this test his Lordship held that the main and dominant purpose of the society before him was to benefit foxhunting and not to benefit the community and that the society was not therefore a charitable society.

Charitable Purposes: Question of Fact or Law.

It was contended in the above mentioned case that the question whether a society is established for charitable purposes or not is a question of fact on which the commissioners' finding is final, but LAWRENCE, J., overruled this contention and said:

"As I read the decisions upon this subject it is for the commissioners to say what are the purposes of the society and for the Court to decide as a matter of law whether those purpose are charitable."

THE

INCOME TAX REPORTS

Vol. IV.

1936

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*[IN THE ALLAHABAD HIGH COURT.]

GOPINATH NAIK

v.

COMMISSIONER OF INCOME TAX, UNITED PROVINCES.

Before Sulaiman, C.J., on difference of opinion between Niamatullah and Bajpai, JJ.

November 22, 1935.

INCOME-TAX—ASSESSMENT BASED ON PRIVATE ENQUIRIES—VALIDITY—INCOME-TAX ENQUIRIES HOW FAR JUDICIAL PROCEEDINGS—APPLICABILITY OF RULES OF EVIDENCE ACT—INDIAN INCOME-TAX ACT (XI OF 1922), SECTIONS 23 (2) & (3) AND 37.

Where an Income-tax Officer, having reason to believe that a return was incorrect and incomplete made private enquiries behind the back of the assessee after starting proceedings under Section 23(3) and made an assessment on the basis of the result of his enquiries, and on appeal, the Assistant Commissioner also made private enquiries and made an assessment on the basis of the result of his enquiries and also relying on the previous year's assessment:

Held by the Court (BAJPAI, J., contra)—(*i*) *that from the stage when the Income-tax Officer serves a notice under Section 23 (2), the proceedings assume the nature of a judicial enquiry and the enquiries made by the Income-tax Officer from the people of the district, after the proceedings under Section 23 (3) had been started, of which no notice had been given to the assessee, were illegal and not authorised by Section 23, sub-section (3) of the Act;* (*ii*) *similarly the enquiries made by the Assistant Commissioner during the hearing of the appeal behind the back of the assessee were not justified by the provisions of sub-section (3) and the result of such private enquiries should not have been made the basis of any assessment;* (*iii*)

on the other hand, there was no objection in the Income Tax Officer and the Assistant Commissioner acting upon the assessment of the previous year if no better evidence was forthcoming, even if the previous year's assessment might have been a best judgment assessment; (iv) that the finding of the Assistant Commissioner so far as it was based on private enquiries was improper and vitiated, but if the finding could be supported on the other relevant circumstances, without taking into account the result of the private enquiries, then the finding would not be illegal according to the principles underlying Section 167 of the Evidence Act.

Held also (BAJPAI, J., dissenting) *that the Assistant Commissioner was not authorised even under Section 13 of the Income Tax Act or otherwise to make private enquiries and to take the result of such enquiries into account in making the assessment.*

Per BAJPAI, J.:—*The Indian Evidence Act with all its details does not apply in the case of an assessment under the Indian Income Tax Act and a margin of approximation is undoubtedly left to the income-tax authorities. Revenue officers have a large discretion to make private enquiries and from the very nature of the proceedings it is apparent that such enquiries are essential. It is, however, necessary that the principles of natural justice should not be violated and the assessee should be permitted to meet the case as revealed by the enquiries:*

Case referred to:

COMMISSIONER OF INCOME-TAX, BIHAR & ORISSA *v.* KAMESHWAR SINGH OF DHARBHANGA [1933] (1 I.T.R. 94; 142 I.C. 437; 12 Pat. 318; A.I.R. 1933 P.C. 108).

Case stated by the Commissioner of Income-tax, Central & United Provinces under Section 66 (3) of the Indian Income-tax Act. [Mis. case No. 97 of 1933].

K. N. Katju and *M. N. Kaul*, for the assessee.
K. Verma, for the Income-tax Department.

This referrence was heard by NIAMATULLAH and BAJPAI, JJ., who differed on both the questions referred by the Commissioner of Income Tax, and the case was then referred to SULAIMAN, C.J.

NIAMATULLAH, J.—This is a reference under Section 66 (3) of the Income Tax Act. The assessee is one Pandit Gopinath Naik of Bakhera Bazaar, District Basti. He submitted a return under

Section 22 (2) for the assessment year 1929-30. The return was not accepted by the Assistant Commissioner, who was empowered to act as an Income Tax Officer. He was assessed at an income of Rs. 1,00,450 including Rs. 1,00,000 as his income from money-lending busineess. He appealed to the Commissioner, who set aside the assessment and directed a fresh assessment. The case was subsequently dealt with by the Income Tax Officer, Basti, who issued a notice under Section 23 (2) directing the assessee to produce his accounts for money-lending business. The accounts were produced, and it was discovered that there were serious omissions which created a strong suspicion that the accounts had been manipulated. An opportunity was given to the assessee to explain certain matters. No explanation was, however, furnished, but a fresh return was submitted. The Income Tax Officer called upon the assessee to substantiate the new return. He also summoned the assessee, who did not, however, appear, nor did he produce any evidence. The Income Tax Officer came to the conclusion that the accounts were "incomplete and unreliable." He estimated the income of the assessee from money-lending business to be Rs. 1,22,000. The estimate was based on calculating the net profits at the rate of 8 per cent. per annum on Rs. 15 lakhs, which was taken to have been invested by the assessee in his money-lending business. The order of the Income Tax Officer and his reasons in support of it appear from Appendix C.

The assessee appealed to the Assistant Commissioner, who agreed with the Income Tax Officer in rejecting the assessee's account books as unreliable. He, however, estimated the amount invested by the assessee in money-lending business to be 11 lakhs only. The Assistant Commissioner based his estimate, partly at any rate, on certain 'enquiries,' of which there is no record and which were admittedly made behind the back of the assessee, from persons supposed to have an idea of the extent to which the assessee had made investments in his money-lending business. His order is Appendix D.

The assessee applied to the Commissioner for revision of the Assistant Commissioner's assessment and for statement of a case being prepared for reference to the High Court. The Commissioner declined to interfere or to make a reference to this Court. The assessee moved this Court under Sec. 66 (3), and the Commissioner was required to prepare a case for the determination of the following two questions:—

(1) Whether the estimate of 11 lakhs as the capital invested by the assessee is based on such evidence as the Assistant Commissioner was in law empowered to act upon ?

(2) Was the Assistant Commissioner authorized under Section 13 of the Income-tax Act or otherwise to make private inquiries and to take the result of such inquiries into account in making the assessment ?

On receipt of this Court's order requiring a statement of the case to be prepared, the Commissioner asked for a report from the Assistant Commissioner as regards the nature of the enquiry made by him and referred to in his order, Appendix B. The report disclosed the fact that the Assistant Commissioner had enquired from the people of Basti about the money-lending business of the assessee. They could not point out any big investment. "Rather they stated that his money-lending business was much like before." The Assistant Commissioner says that he was led by what the people of Basti had stated to him to conclude that the Income Tax Officer's estimate of the assessee's investment, namely, 15 lakhs, was excessive, and so he reduced it to 11 lakhs, because the assessee had been assessed in the year immediately preceding on an income of one lakh based on investments amounting to 10 lakhs in the money-lending business. In accepting that exemplar he was influenced by the fact that the assessee had taken no exception to it. The additional sum of one lakh, which brought the total to 11 lakhs estimated by him, was due to the fact that he had discovered certain omissions in the assessee's accounts. One of the questions argued before us was whether the report of the Assistant Commissioner, above referred to, can be accepted as a supplement to his order, Appendix B, by which he had estimated that the assessee had invested 11 lakhs in his money-lending business. We think that the report may be accepted as an explanation of certain obscure portions of his order of assessment, which by itself does not clearly show the data on which he proceeded.

The first question raises a point of some nicety and of not a little difficulty. In the present case the Assistant Commissioner based his assessment on the estimated amount of the assessee's investment in money-lending business, assumed to yield a profit of 8 per cent. per annum. The estimate itself is based on the amount of investment assumed in the year immediately preceding and the result of his enquiry at Basti. I use the word "assumed" deliberately, because in that year the assessment was one under Section 23 (4)

that is to say, a best judgment assessment, the assessee not having complied with a notice requiring him to submit a return. For the present year the assessee complied with the notice and furnished a return. Though the Income Tax Officer did not accept the return as correct, he made the assessment not under Section 23 (4) but under Section 23 (3).

In my opinion there is an essential difference between cases in which action is taken under Section 23 (3) and those under Section 23 (4). I do not pause to consider the question whether the Income Tax Officer could have proceeded under Section 23 (4) in the present case, as he protessed to act under Section 23 (3). Where a return is furnished, but is considered by the Income Tax Officer to be incorrect or incomplete, he is to serve a notice on the assessee requiring him on a date to be therein specified either to attend the Income Tax Officer's office or to produce, or cause to be produced any evidence on which the assessee may rely in support of his return. Section 23 (3) provides that on the day so specified

"the *Income Tax Officer, after hearing such evidence as such person may produce and such other evidence as the Income Tax Officer may-require*, on specified points, shall, by an order in writing, assess the total income of the assessee, and determine the sum payable by him on the basis of such assessment."

The important question, which arises in this connection, is whether if the return is found to be incorrect or incomplete and the assessee produces no evidence, it is open to the Income Tax Officer to assess the income in any manner he thinks fit, or whether the assessment must proceed on some 'evidence'. It is argued by the learned advocate for the income tax department, that there is nothing in Section 23 (3) which makes it incumbent on the Income Tax Officer to base his assessment on "evidence" whatever it may mean. It is pointed out that Section 23 (3), as it stands, merely makes it obligatory that the evidence, which the assessee may produce or the Income Tax Officer may call for, should be heard, but that if no such evidence is produced by the assessee nor is any called for by the Income Tax Officer, himself, it is open to him to make the assessment on such basis as he thinks fit. If this line of argument is accepted, an assessment, made under Section 23 (3), will, in many cases, be virtually, an assessment under Section 23 (4), *i.e.*, best judgment assessment which may be based on pure conjecture. This kind of assessment is, however, allowed only in cases falling within the purview of

Section 23 (4), *i.e.*, where the assessee fails to make a return or fails to produce his accounts, when required to do so, or fails to comply with all the terms of the notice under Section 22 (4). In the present case, these conditions were *ex hypothesi* absent. and the Income Tax Officer did not proceed under Section 23 (4). It follows that a case for assessment to the best of judgment of the Income Tax Officer did not exist. It seems to me that, where the Income Tax Officer acts under Section 23 (3) the assessment must be based on 'evidence'. The obligation to hear evidence which may be produced by the assessee or may be called for by the Income Tax Officer himself is a clear index to the further obligation to "determine the sum payable by" the assessee on the basis of the evidence adduced in the case. Where the assessee himself does not produce any evidence, the Income Tax Officer cannot be at a loss to make the assessment, because the law has given him ample powers to call for evidence. Section 37 of the Act empowers him to enforce the attendance of any person and to examine him on oath or affirmation, compel the production of documents and to issue commission for the examination of witness. Where the assessee himself does not produce any evidence, comparatively slight evidence, coupled with the inference drawn from the conduct of the assessee, will be enough, for compliance with the requirements of Section 23 (3).

The next question is as to what is meant by the word "evidence" used in Section 23 (3). It is not defined in the Income Tax Act itself. So far as I have been able to ascertain, no rules have been made under Section 29 laying down what should be considered to be evidence for the purpose of assessment. I think that, on the one hand, the Legislature did not intend that the evidence on which income tax authorities are to act, should be evidence which fulfils all the technical requirements of the Indian Evidence Act, on the other hand mere conjecture, surmise or assumption of a fact, as distinguished from inference from proved circumstances, does not amount to evidence within the meaning of Section 23 (3). Where the Income Tax Officer bases his assessment on the statements of witnesses, they should be produced before him "on the day specified in the notice issued under Sub-section (2)," *i.e.*, the day on which the assessee is to attend and to produce his evidence, which implies that the evidence should be "produced" in his presence. Whether the evidence should be in every case on oath and be in accordance with the rules of relevancy laid down in the Indian Evidence Act are questions which

do not call for decision in the present case. It is enough to say, for the purpose of this case, that the result of the enquiry made by the Assistant Commissioner from certain residents of Basti in the absence of the assessee is not evidence within the meaning of Section 23 (3). The only other ground, on which the Assistant Commissioner based his assessment is that, in the year immediately preceding, the assessee's investment had been found to be 10 lakhs. As already mentioned, in that year the assessment was under Section 23 (4), *i.e.*, best-judgment assessment, which need not have been based on evidence. There no appeal is allowed from such assessment which may be based on no data or may be arbitrary. If a mere conjecture, surmise or assumption, however shrewd, is no "evidence" within the meaning of Section 23 (3), as I hold, such conjecture, surmise or assumption, made in the previous year under Section 23 (4) can be no more evidence. There is nothing to show that the assessment for the last year which was a "best-judgment" assessment was based on any known data. It was a conjecture or assumption, which the Income Tax Officer was entitled to make in view of the assessee's conduct. The assessee's conduct this year, though open to objection otherwise is admittedly not such as to justify assessment of that kind. The Income Tax Officer should have based it on "evidence" as required by Section 23 (3). It was open to the Income Tax Officer to have relied on the records of several past years which were in his possession. It is not disputed that the assessee was assessed for several years in the ordinary course, and not under Section 23 (4); and if the Income Tax Officer had taken those assessments as a guide, it could not have been said that his assessment for the year in question was based on no evidence.

The Commissioner contends in his remarks made in the statement of the case:

'The Assistant Commissioner's estimate of the investment is, however, based, not on the result of those inquiries, but on other data. These data were furnished by the assessment for the year 1928-29, the year immediately preceding the assessment year in dispute, in which the total investment was estimated by the Income Tax Officer of the time at 10 lakhs and the estimate was accepted by the assessee without a demur and without having recourse to the remedy provided by Section 27 against a best judgment assessment under Section 23 (4)'.

A "best judgment" assessment remains what it is even though the assessee may not 'demur' or may have no recourse to

the remedy provided by Section 27. Moreover, all that the assessee could have done under Section 27 was to offer to satisfy the Income Tax Officer

'that he was prevented by sufficient cause from making the return required by Section 22, or that he did not receive the notice issued under Section 22 (4) or Section 23 (2), or that he had not a reasonable opportunity to comply, or was prevented by sufficient cause from complying, with the terms of the last-mentioned notices...........'

His failure to satisfy the Income Tax Officer on any of the matters referred to in that section can throw no light on the arbitrary character or otherwise of the best judgment assessment. It should be noticed that an application under Section 27 is not aimed at the merits of assessment, but has reference to wholly collateral matters.

The Commissioner further observed that:

'The estimate itself is, in the Commissioner's opinion, founded on adequate grounds which have not been rebutted by any evidence produced by the assessee. In using this language to convey his reply to the first question, the Commissioner desires, very respectfully to point out that the wording of the question is such that it might be read as implying that a greater burden of proof is thrown upon the income tax authorities than the law itself prescribes. The scheme of the Act, as will be clearly seen from the wording of sub-Section (2) of Section 23, is that if the Income Tax Officer has *bona fide* grounds for holding a certain belief, he must give the assessee an opportunity of producing evidence to rebut that belief; but subject to such evidence, the burden of producing which is on the assessee, it is not necessary that the materials on which the income tax authority bases his belief should have the formality of judicial evidence'.

I am unable to concur with the Commissioner in the view he takes of the scheme of the Act. It is true, Section 23 (2) provides that, where the Income Tax Officer has reason to believe that a return is incorrect or incomplete, he may call upon the assessee to substantiate it and that, to that extent, the onus lies on the assessee. It could not be otherwise. The assessee alleges by his return that his assessable income is what is stated therein. But the Income Tax Officer denies that fact. The onus is undoubtedly on the assessee, if he maintains that his return is correct; but if the return is set aside and the Income Tax Officer puts forward an

affirmative case that the assessee's income is more and gives a definite figure, the onus is on him to support his case. It cannot be said that the onus lies on the assessee not only to substantiate his return but also to disprove every allegation or assertion which the Income Tax Officer may choose to make. This is clear from Section 23 (3) which makes it incumbent on the Income Tax Officer to make the assessment "after hearing such evidence as such person may produce and such other evidence as the Income Tax Officer may require on specified points." That part of the section obviously means that the Income Tax Officer shall hear the evidence which the assessee may produce in support of his return, and that if the return or the evidence in support thereof is not accepted, the Income Tax Officer shall hear such further evidence as may be necessary for making the assessment. The words "may require" refer to his requirements in making the assessment and not to evidence which he may call for. It is clear to my mind that the section contemplates that if the evidence adduced by the assessee is not accepted, the Income Tax Officer must have recourse to other evidence to base his assessment on. It does not place the Income Tax Officer absolutely on the defensive, so that, if the assessee's attempt to substantiate his return fails, the Income Tax Officer can assume the income of the assessee to be anything which his imagination may lead to.

Reliance was placed by the learned advocate for the Commissioner on the following observation occurring in *The Commissioner of Income Tax, Bihar and Orissa* v. *Kameshwar Singh of Darbhanga:*

'In the High Court the Chief Justice (COURTNEY-TERRELL) after pointing out that the question is one of quantum only says :— Learned counsel for the assessee has argued that the officer is not entitled to make a guess without evidence, and I agree with that contention, but in this case the state of affairs in the previous years, coupled with the fact that the assessee had a large mortgage loan business and must have enforced mortgages by sale on many occasions, afford ample material for the assessment made. I would answer the question in the affirmative. The other Judges concurred, and their Lordships also agree, adding only that if the assessee wished to displace the taxing officer's estimate, it was open to him to adduce evidence of all his purchase transactions during the year and of the financial results thereof, which he apparently made no attempt to do.'

It is argued that their Lordships have laid down the rule that the Income Tax Officer is to make an estimate, and the onus is thrown on the assessee to disprove that estimate. The observation must be considered in the light of the facts of that case which was one in which the assessee's return was out of the question. The Income Tax Officer had made an estimate, which was based on evidence. The Chief Justice clearly pointed out that the estimate was based on evidence, as it should have been. He clearly says that the Income Tax Officer is not entitled to make a guess without evidence; but he found that the guess (which amounts to estimate if there is evidence in support of it), was, in that case, borne out by the evidence, and the only question was one of quantum. Their Lordships approved of this view and held that the assessee should have adduced evidence to rebut the estimate. It seems to me that the case was one in which the initial onus resting on the Income Tax Officer (the return being ignored) was discharged, and a case existed for the assessee to rebut the estimate made by the Income Tax Officer. I think that the case quoted above does not support the contention put forward on behalf of the department.

In the present case, if instead of 15 or 11 lakhs, the Income Tax Officer or the Assistant Commissioner had taken the assessee's income to be 50 lakhs he would have had no means of rebutting that assumption. In my opinion to countenance the rule contended for by the Commissioner will lead to highly undesirable results.

For the reasons explained above, I answer the first question in the negative. The answer to the second question will, in a great measure, follow from that to the first. Section 13 merely provides for methods of accounting. It throws no light on the main question in the case as to whether the result of private enquiries made by the Assistant Commissioner is or is not evidence for the purpose of Section 23 (3). I answer the second question also in the negative.

BAJPAI, J.—In this case under Section 66 (3) of the Indian Income Tax Act the High Court, after the refusal of the Commissioner to state a case on the assessee's application, required the Commissioner to state a case and to refer it by an order dated October 27, 1933. The Commissioner was directed to prepare a case for the determination of the following questions of law :—

(1) Whether the estimate of eleven lakhs as the capital invested by the assessee is based on such evidence as the Assistant Commissioner was in law empowered to act upon?

(2) Was the Assistant Commissioner authorised under Section 13 of the Income Tax Act or otherwise to make private enquiries and to take the result of such enquiries into account in making the assessment?

It is necessary to state the facts in some detail. For the assessment year 1929-30 the Assistant Commissioner of Income Tax of Benares who had been empowered under Section 5 (4) of the Income Tax Act to deal with the case as an Income Tax Officer, after rejecting the accounts produced by the assessee, assessed the amount of his income at Rs. 1,00,450 by his order dated March 6, 1930. The Commissioner on appeal by his order dated August 1, 1930, set aside the assessment and directed that a fresh assessment be made and the Income Tax Officer was required specifically to deal with the following points :—

(1) Whether the accounts can be computed as complete or whether they should be rejected as incomplete?

(2) In case the accounts are rejected as incomplete what should be estimated as the assessee's income from money-lending?

It may be mentioned that the Assistant Commissioner had estimated the income from money-lending as one lakh.

By this time the Income Tax Officer of Basti was a full powered officer and it was not necessary for the Assistant Commissioner to deal with the matter.

A fresh notice was issued under Section 23 (2) and in compliance with that notice the assessee produced certain accounts for the money-lending business. In the Income Tax Officer's opinion there were several omissions in the books and they were pointed out to the assessee's representative who admitted the mistakes and requested for an adjournment in order to enable him to explain the omissions. The case was postponed to March 17, 1931 and at the same time the Income Tax Officer under Section 23 (3) asked for evidence on specified points. No evidence was produced on this date nor was any explanation offered, but a fresh return was received through the post. On receipt of this return the Income Tax Officer issued a fresh notice on April 20, 1931 under Section 23 (2) requiring the assessee to produce evidence in support of the revised

return, and at the same time he issued a summons under Section 37 of the Income Tax Act for the personal attendance of the assessee. The date fixed for this purpose was April 30, 1931. On May 2, 1931 the assessee sent a letter that he had no evidence to produce beyond the account books which had already been produced before the Income Tax Officer, and as regards his personal attendance he requested that the case might be postponed to some date in June. The Income Tax Officer could not postpone the case to June but fixed May 13, 1931 for hearing. The assessee once again sent a petition by post repeating that he could not produce any other evidence except the accounts which were already in the possession of the Income Tax Officer. The Income Tax Officer then on the same date wrote a letter to the assessee warning him that if the summons under Section 37 and the notice under Section 23 (2) were not complied with by May 18, 1931, he would be compelled to hold adversely to the assessee that the revised return was not a return under Section 22 (3) and that the income stated therein was not based on the accounts produced. There was no compliance, but an application was received on June 1, 1931 by which the assessee asked for an adjournment to some date after June 8. The Income Tax Officer allowed one more opportunity and postponed the case to June 8. The assessee failed to attend or produce evidence.

The Income Tax Officer then on that date proceeded to assess the income of the assessee. He in his judgment pointed out various omissions, falsehoods and concealments and observed:

'Taking all these facts into consideration it is difficult for me to accept the books produced by the assessee. No income can be deduced from them. I feel convinced that they are incomplete and fictitious.'

He then turned his attention towards the computation of the income of the assessee. He said:

'The total investment of the assessee according to the books produced before me comes to about 5 lakhs only. But my predecessor in the year 1928-29 estimated a total investment of 10 lakhs. The assessee himself never disclosed his entire investment and in the year Samwat 1984, for which 10 lakhs were estimated, he showed a total investment of Rs. 2,70,231 only. This figure can give some idea of the extent to which, as a matter of habit, he is prone to conceal. When, however, my predecessor made the estimate of 10 lakhs on the material available to him he was not

aware of the investments to the extent of about 2 lakhs, which have now been incorporated in the books of Samvat 1985 through the personal account of Pandit Gopi Nath. At least there is nothing on the record to show that he was aware. Over and above these as is shown in the course of this order, the assessee has at least concealed an investment of Rs. 11,735 on which Rs. 704 were credited as interest against Tribeni Chippi. The record of the assessee is not very clean. There has not been any single assessment in any year which has been made on the basis of his books. Penalty under Section 28, too, was imposed in one year. Concealments are discovered every year, and the books have to be rejected. In fact in the year 1928-29 after some concealments were discovered, he promised to my predecessor, as is apparent from his order, that he would in future produce the correct books. He has not fulfilled this promise. This year I have made detailed inquiries at Bakhera and the neighbouring places and also at Gorakhpur, the district in which the assessee has considerable investment. I am told that advances are made in the villages in the districts of Gorakhpur and Basti and they are never shown in the books produced before us. His total investment is, in my opinion, of about 15 lakhs. The rate of interest charged by the assessee of course varies with the particular investment. It sometimes is in the neighbourhood of 24 per cent. But at the same time there are loans, I am told, in which the rate of interest is so low as 6 per cent. I, therefore, think it to be fair if I take an income of Rs. 1,20,000 from money-lending.'

It would thus appear that the estimate made by the Income Tax Officer was based on the fact that the estimate of the previous year by the former officer was 10 lakhs, that the previous order did not show that the officer was aware of investments to the extent of about 2 lakhs, that some further concealments had been discovered, that the record of the assessee was not clean, that the promise to produce the correct books was not redeemed, and that the assessee had the reputation of a big money-lender. This reputation was based as far as one can gather on private enquiries. There was an appeal and the Assistant Commissioner went into the matter in detail and he also came to the conclusion that

" in view of the omissions and irregularities discussed above, it is clear that the books of Samvat 1985 are not complete and do not reflect the entire income of the appellant. Therefore, the Income Tax Officer was justified in rejecting them and not basing his assessment on them."

He then proceeded to consider whether the estimate of an income of Rs. 1,20,000 made by the Income Tax Officer from money-lending business was a fair one. He said:

"The Income Tax Officer has estimated the total investment of the appellant at about 15 lakhs against 10 lakhs estimated previously. The partial account books of the appellant show his investments at a little under 6 lakhs, and the amounts of concealment discovered do not warrant the estimate of investment at such a high figure as 15 lakhs I have also made enquiries and taking all the circumstances of the case into consideration, it would be fair to estimate his investments at 11 lakhs."

The income from this capital at the average rate of 8 per cent. which appeared to the Assistant Commissioner a fair one was fixed at Rs. 88,000 against Rs. 1,20,000 determined by the Income Tax Officer.

The assessee then requested the Commissioner to state a case to the High Court under Section 66 (2); the Commissioner of Income-tax by his order dated August 24, 1922 refused to state a case, but on the assessee's application the High Court required the Commissioner to refer a case and this, as mentioned before, has been done now. The Commissioner asked the Assistant Commissioner to report on the question as to how the estimate at 11 lakhs as the capital invested by the assessee was made, and in his report dated December 20, 1933 he says:

"The assessee was assessed on March 30, 1929, for the year 1928-29 on Rs. 1,00,300 including an income of 1 lakh from business on estimated investments of about 10 lakhs. No exception was taken to this assessment by the assessee. A loan of Rs. 11,018-15-6, together with Rs. 716-9-3 on account of interest on Rs. 11,735 in round figures due from one Tribeni Ram Chhipi of Gorakpur was found missing from the books of the assessee. Some omissions and discrepancies were also found out as discussed by me in my appellate order of February 29, 1932. On account of these omissions I added 1 lakh to the investments of 10 lakhs as were estimated before, which was a good evidence. Thus I determined his total investments at 11 lakhs."

The learned Commissioner is of the opinion that an estimate of 11 lakhs as the capital invested by the assessee is based on such evidence as the Assistant Commissioner was in law empowered to act upon. It has been argued before us by the assessee that there

was no basis in law for the estimate made by the Assistant Commissioner.

Various considerations arise in connection with the first question formulated by us. Under Section 3 of the Indian Evidence Act a Court includes all persons except arbitrators legally authorised to take evidence and in view of Section 37 of the Income Tax Act, Income Tax Officers, Assistant Commissioners and Commissioners may be said to be a Court. But the Evidence Act applies only to "judicial proceedings" and under Section 37 a proceeding before an Income Tax Officer, Assistant Commissioner or Commissioner shall be deemed to be a "judicial proceedings" within the meaning of Sections 193 and 228 and for the purposes of Section 196 of the Indian Penal Code. It will, therefore, appear that the proceedings before the various Revenue Officers mentioned above are "judicial proceedings" to a limited extent only and they are courts under the Civil Procedure Code to a limited extent only, namely, to the extent indicated by Section 37. If an Income Tax Officer in making an investigation was a Court, and, if proceedings before him were judicial proceedings, for all purposes, then there was no necessity for enacting Section 37. It is reasonable to hold that on the principle of *expressio unius est exclusio alterius* such proceedings are not judicial proceedings for other purposes, and there can be little doubt that the detailed provisions of the Indian Evidence Act will not apply to such proceedings, and this is obvious because the same person cannot be a party, judge and witness in his own case. This is made further clear from the fact that under Section 23 (4) the Income Tax Officer has perforce to assess to the best of his judgment, and in that case, although the Income Tax Officer is not entitled to make an assessment capriciously and arbitrarily but by honest means and in honest spirit, yet at the same time he cannot adopt lawyer-like methods and follow the strict provisions of the Indian Evidence Act.

Under Section 13 of the Indian Income Tax Act if no method of accounting has been regularly employed or if the method employed is such that in the opinion of the Income Tax Officer, the income, profits and gains cannot properly be deduced therefrom, then the computation shall be made upon such basis and in such manner as the Income Tax Officer may determine. The provision also shows that when the method adopted by the assessee has been rejected by the Income Tax Officer then he is entitled to adopt a different basis and a different method. Under Section 31 (2)

the Assistant Commissioner may before disposing of any appeal make such further enquiry as he thinks fit or cause further enquiry to be made by the Income Tax Officer. The scope of such an enquiry is not fettered by any limitations. It is, therefore, clear to my mind that the Indian Evidence Act with all its details does not apply in the case of an assessment under the Indian Income Tax Act, and a margin of approximation is undoubtedly left to the income tax authorities, specially when the assessee has been guilty of contumacy. In *Commissioner of Income Tax, Bihar and Orissa* v. *Kameshwar Singh of Darbhanga* their Lordships of the Privy Council quoted the following passage from the judgment of the learned Chief Justice of Patna:

"Learned counsel for the assessee has argued that the officer is not entitled to make a guess without evidence and I agree with the contention, but in this case the state of affairs in the previous years coupled with the fact that the assessee had a large mortgage loan business and must have enforced mortgages by sale on many occasions afford ample material for the assessment made. I would answer the question in the affirmative."

and then their Lordships proceed and say that with this observation of the Chief Justice:

"the other Judges concurred and their Lordships agree adding only that if the assessee wished to displace the taxing officer's estimate it was open to him to adduce evidence of all his purchase transactions during the year and of the financial results thereof which he apparently made no attempt to do".

Under circumstances like these the Income Tax Officer has to proceed upon the principles of natural justice. In the present case the Assistant Commissioner when disposing of the appeal by his order dated February 29, 1932 had before him the order of the Income Tax Officer which had stated the circumstances of the case and from which I have quoted in extenso in an earlier portion of my judgment. He based his estimate on the fact that the partial account books of the appellants showed his investment at a little under 6 lakhs. He also took into consideration the fact that there were certain concealments, that no assessment in any previous year had been made on the basis of his books, that he had not fulfilled the promise of producing correct books and the fact that the assessment of the previous year upon a money-lending business of 10 lakhs had not been challenged in any manner available to the assessee. He also paid due regard to the fact that the *ex parte* detailed enquiries

made by the Income Tax Officer showed that advances made in the districts of Gorakhpur and Basti were never shown in the books. He then came to the conclusion that taking all the circumstances of the case into consideration it would be fair to estimate his investments at 11 lakhs.

He makes the basis of his estimate further clear by his report dated December 20, 1933, which has been quoted in an earlier part of my judgment. I have no reason to doubt his statement contained in his report and I see no reason to accept the contention of the counsel for the assessee that the Assistant Commissioner of Income Tax, when he says that he took into consideration the fact of the previous year's assessment, took his cue from the argument of the Crown counsel advanced before us when the question of asking the Commissioner to state a case was under consideration.

His original appellate order clearly shows that he took all the circumstances of the case into consideration and he now definitely states that he took this factor into account. I am, therefore, of the opinion that in the peculiar circumstances of the case the estimate of 11 lakhs as the capital invested by the assessee is based on such evidence as the Assistant Commissioner was in law empowered to act upon, and my answer to the first question is in the affirmative.

As regards the question I have already said, when discussing the first question, that the Revenue Officers have a large discretion to make private enquiries and from the very nature of the proceedings it is apparent that such enquiries are essential. It is, however, necessary that the principles of natural justice should not be violated and the assessee should be permitted to meet the case as revealed by the enquiries. In the present case opportunity after opportunity was given to the assessee and he was asked to produce his books and to attend in person. His representative on one occasion admitted that omissions had been made and asked for time to explain them. No explanation was ever offered and the Assistant Commissioner in his report dated December 20, 1933, says that he used the result of his enquiry in favour of the assessee by reducing the estimate of the Income Tax Officer. My answer to the second question, therefore, is that the Assistant Commissioner was authorised under Section 13 of the Income Tax Act and also otherwise to make private enquiries, but he is not permitted to take the result of such private enquiries into account in making the assessment without giving an opportunity to the assessee to

meet them and (in the words of their Lordships of the Privy Council) "to displace the Taxing Officer's estimate".

NIAMATULLAH and BAJPAI, JJ.—As the Judges composing this Bench differ on both the questions referred by the Commissioner, the case will be laid before the Hon'ble Chief Justice for a reference under Section 98, C. P. C., to another Judge or a larger Bench.

The case was then heard by SULAIMAN, C.J., who delivered the following judgment:—

SULAIMAN, C.J.—This case has been referred to a third Judge because of a difference of opinion between the two learned Judges who heard this reference under Section 66 of the Income Tax Act.

The two questions for consideration are as follows:—

(1) Whether the estimate of 11 lakhs as the capital invested by the assessee is based on such evidence as the Assistant Commissioner was in law empowered to act upon?

(2) Was the Assistant Commissioner authorised under Section 13 of the Income Tax Act or otherwise to make private inquiries and to take the result of such inquiries into account in making the assessment?

It appears that for the year 1928-29 (corresponding to 1984 *Samvat*), the assessee was assessed on the basis of a capital investment in money-lending business amounting to 10 lakhs. This assessment was based on the best judgment estimate made in the absence of any evidence produced by the assessee.

For the year 1929-30 which is the year in dispute in this case, the assessee submitted a return for Rs. 29,810 which was considerably below the estimated income of the previous year. The Assistant Commissioner considered the return to be incorrect and incomplete and issued notice under Section 23 (2) to the assessee to attend at the office or produce any evidence on which he might rely in support of the return. The assessee appeared and produced certain account books after information was called for by the Assistant Commissioner under a fresh notice issued under the sub-section. Afterwards on March 6, 1930, the Assistant Commissioner, the Income Tax Officer not being empowered at that time, made the assessment on an income of one lakh from money-lending business. On appeal the Commissioner of Income Tax set

aside the assessment and sent the case back with certain directions. A fresh notice was accordingly issued by the Income Tax Officer, who then became invested with the necessary powers, under Section 23 (2) and the statement of the assessee was recorded. The account books produced by him were again examined and then a fresh notice under Section 23 (3) was issued to him on March 16, 1931. The assessee submitted a revised return, but the Income Tax Officer was still not satisfied and issued a fresh notice under sub-section (2) for further information as well as for personal attendance. There were some adjournments of the hearing when another notice under sub-section (3) was issued on May 19, 1931, for further particulars on specific points. Ultimately on June 8, 1931, the Income Tax Officer made an assessment on the basis of a capital investment of 15 lakhs and calculating the income at the rate of 8 per cent. per annum fixed Rs. 1,20,000 as the income from the money-lending business. The learned Income Tax Officer found fault with the account-books produced by the assessee and considered them incomplete and unreliable and did not act upon them. In the course of his order he remarked:

'This year I have made detailed inquiries at Bakhera and the neighbouring places and also at Gorakhpur, the district in which the assessee has considerable investment. I am told that advances are made in the villages in the districts of Gorakhpur and Basti and they are never shown in the books produced before us. His total investment is, in my opinion, of about 15 lakhs.'

When the matter went up in appeal before the Assistant Commissioner, no ground seems to have been taken against the Income Tax Officer making private enquiries, but a ground was taken that the estimate based on rumour or private information in a vague and fanciful way was *ultra vires*. There were several hearings before the Assistant Commissioner. He also seems to have acted under Section 31 of the Income Tax Act in making further enquiries and taking some evidence. Statements of the assessee and at least of one witness were recorded and certain books were also examined. The appeal was ultimately disposed of on February 22, 1932, by an order under which the capital investment was reduced from 15 lakhs to 11 lakhs, but the average rate of 8 per cent. was maintained. In view of the omissions and irregularities pointed out by him, it was clear that the account books of the assessee were not complete and did not reflect the entire income of the appellant, and accordingly the Income Tax Officer was justified

in rejecting them and not basing his estimate on them. In proceeding to consider whether the estimate of the income of Rs. 1,20,000 made by the Income Tax Officer from money-lending was a fair one, the learned Assistant Commissioner remarked:

'The Income Tax Officer has estimated the total investment of the appellant at about 15 lakhs against 10 lakhs estimated previously. The partial account books of the appellant show his investments at a little under 6 lakhs, and the amounts of concealment discovered do not warrant the estimate of investments at such a high figure as 15 lakhs. I have also made enquiries and taking all the circumstances of the case into consideration, it would be fair to estimate his investments at 11 lakhs. It is now ascertained that the bulk of his loans carry interest from 6 per cent. to 9 per cent. per annum and only small loans bear 24 per cent per annum.'

On an application made by the assessee the Commissioner declined to state the case for the High Court, but on a further application made to the High Court, a Bench of this Court by their order dated October 27, 1933, asked the Commissioner to state the case on the two points quoted at the outset. In compliance with this order the case has been stated by the Commissioner. The Bench in the course of their order had directed that in preparing the statement of the case, it should be clearly shown whether any, and if so, what enquiries were made by the Assistant Commissioner behind the back of the assessee, as his reference to enquiries was somewhat vague and in the context in which it occurred it gave the impression that he made enquiries behind the back of the assessee.

The first question which has been argued before me at the bar is whether it would be proper to take into account the subsequent explanation furnished by the Assistant Commissioner as directed by this Court. The Assistant Commissioner in his explanation has said:

"I enquired from the people of Basti about the money-lending business of the assessee. They could not point out to me any big investments, rather they stated that his money-lending business was much like before. This led me to conclude that the Income Tax Officer's estimate of the assessee's investments of 15 lakhs was excessive despite the fact that he gave reasons for estimating them at 15 lakhs."

He then proceeded to give reasons why he kept the investments at 11 lakhs, emphasizing his reliance on the previous estimated

investment of 10 lakhs and additions made thereon on account of certain discrepancies in the books.

I do not think that it would be appropriate to take into account the explanation of the Assistant Commissioner detailing the reasons on which he proceeded in order to make the assessment at 11 lakhs. His explanation of the nature of the enquiry made by him was, of course, in response to the suggestion made by this Court. The propriety or otherwise of the order of assessment made by the Assistant Commissioner must depend on the order as it stands irrespective of additional reasons that have been given by him subsequently.

No question arises before me as to whether the assessment of income tax on the basis of interest accrued on investments, even though not realised, because it was stated that the accounts were kept on a mercantile accountancy basis, was correct. I, therefore, express no opinion on this point.

The principal question for decision is whether the private enquiries made by the Income Tax Officer and the Assistant Commissioner were proper and the result of such inquiries could be taken into consideration by them in making the assessment. It seems to me that under Section 23 when a return is received by an Income Tax Officer, he is not bound to accept it as correct and complete. He is entitled to make enquiries as to whether there is reason to suspect that return is incorrect or incomplete. He can also look into the previous assessments and consider whether there is any serious ground for suspicion. All such acts done by him are in the nature of administrative acts and in my opinion no objection can be taken to such private enquiries which must, of necessity, be carried on behind the back of the assessee and even before he has any notice that such enquiries are being made.

If the Income Tax Officer is satisfied that the return is correct and complete, he has to proceed under sub-section (1) of Section 23. He has to assess the income of the assessee on the basis of the return. If however, he has reason to believe that the return is incorrect and incomplete, he has to serve notice under sub-section (2) of that section on the assessee specifying a date and calling upon him to attend at his office or produce any evidence on which he may rely in support of his return. From this stage the proceeding assumes the character of a judicial enquiry, although not conducted by a judicial officer. The Income Tax Officer has to make up his mind as to whether the return is incorrect

and should be relinquished and, if so, what should be the proper assessment.

Under sub-section (3) of this section the Income Tax Officer has to hear such "evidence" as the assessee may produce and "such other evidence as the Income Tax Officer may require" on specific points; and he has then to assess the income and determine the sum payable by the assessee on such basis. Now Section 37 of the Act empowers the Income Tax Officer to enforce the attendance of persons and examine them on oath or affirmation, compel the production of documents and issue commissions for the examination of witnesses. All these are matters which have necessarily to be resorted to in the presence of and within the knowledge of the assessee. Sub-section (3) of Section 23 speaks of the Income Tax Officer hearing such other evidence as he may require that is to say, evidence other than that produced by the assessee which the Income Tax Officer considers necessary to take, but the word used is "evidence" and not other words, like, information. It would seem to follow *prima facie* that what the sub-section authorizes the Income Tax Officer to do is to take evidence in rebuttal of the evidence produced by the assessee and which *prima facie* should be taken in the presence of the assessee and of which the assessee should have knowledge in order that he may be able to meet such evidence.

On the other hand, sub-section (4) of Section 23 makes an entirely different provision. Where the assessee fails to make a return or fails to comply with all the terms of the notices issued to him, the Income Tax Officer "shall make the assessment to the best of his judgment." Here there is no question of his taking any further evidence nor is there any necessity for him to take any evidence at his own instance. The penalty prescribed for failing to make the return or for failure to comply with the terms of a notice is that the matter is left to the final discretion of the Income Tax Officer to make the best of the assessment he can and his order is final and no appeal lies therefrom.

Obviously there ought to be a difference between a case where a further appeal is allowed and a case where no such appeal lies. Where an appeal lies to a higher Court, it would be inappropriate that the Income Tax Officer's assessment should be based on the result of private enquiries made by him behind the back of the assessee, of which no record is kept, for such materials would be before the appellate Court

which has to exercise its own judgment in seeing whether the assessment is correct or not correct. On the other hand, where the Income Tax Officer's order is to be final, there is no such necessity, though there is a remedy by way of getting this order set aside if sufficient cause is shown.

Now the provisions of Section 23 apply to the Income Tax Officer just as much as they would apply to the Assistant Commissioner in hearing an appeal. It would, therefore, follow that even though the order of the Assistant Commissioner is final on facts, he also would not be competent to make private enquiries behind the back of the assessee and collect information which the assessee has no opportunity to meet. It, therefore, seems to me that the enquiries made by the Income Tax Officer from the people of the district, after proceedings under Section 23 (3) had started, of which no notice had been given to the assessee, were illegal and not authorized by sub-section (3). Similarly, the enquiries made by the Assistant Commissioner during the hearing of the appeal behind the back of the appellant were not justified by the provisions of sub-section (3) and the result of such private enquiries should not have been made the basis of any assessment.

On the other hand, I see no objection in the Income Tax Officer or the Assistant Commissioner acting upon the assessment for the previous year if no better evidence is forthcoming. An Income Tax Officer, and for the matter of that, an Assistant Commissioner is not bound to accept either the correctness of the return or the genuineness and completeness of the account-books produced before him or the truth of the evidence produced by the assessee. If he has ground for believing that such evidence is untrustworthy, he can certainly reject it. Having rejected such evidence it is open to him to pursue the enquiry further and take more evidence which he considers necessary; but he is not bound to do so. In the absence of any better evidence he is certainly entitled to fall back on the assessment of income made during the previous year even though that assessment might have been the best judgment estimate. The fact that during the previous year the income was assessed on a certain figure is certainly some evidence on which he can proceed, even independently of any presumption of continuity. If the assessee fails to produce satisfactory evidence, he fails to displace the previous year's estimate, which is certainly admissible against him.

In this view of the matter I am of the opinion that the finding of the Assistant Commissioner was passed partly on the

result of private enquiries made by him and partly on the admitted circumstances of this case. So far as it was based on the private enquiries it was improper and is vitiated. But if it could be based on the other circumstances, without taking into account the result of the private enquiries, then the finding would not be illegal according to the principle underlying Section 167 of the Indian Evidence Act. I am not called upon to say whether in this particular case the assessment at 11 lakhs could have been made on the other circumstances of this case excluding the result of the private enquiries. This is for the Assistant Commissioner to decide.

My answer to the first question is that the estimate was based on evidence which the Assistant Commissioner was partly empowered to act upon and partly not empowered to act upon, and my answer to the second question is in the negative.

This being my opinion on the two questions that arise in this case and on which the learned Judges have differed, let the case go back to the bench for final disposal.

On receipt of the opinion of SULAIMAN, C. J., the Division Bench passed the following order :—

NIAMATULLAH and BAJPAI, JJ.—Having regard to the decision of the Hon'ble Chief Justice, to whom the case was referred in view of the difference of opinion between the judges composing this bench, the two questions, which are the subject of reference under Section 66 of the Income Tax Act, are answered as follows :—

(1) The estimate of 11 lakhs as the capital invested by the assessee is based partly on such evidence as the Assistant Commissioner was in law empowered to act upon and partly on evidence which he was not empowered by law to act upon.

(2) The Assistant Commissioner was not authorized under Section 13 of the Income Tax Act or otherwise to make private enquiries and to take the result of such enquiries into account in making the assessment.

As regards costs, we direct that the department should pay three-fourths of the costs incurred by the assessee and that the assessee should pay one-fourth of the costs incurred by the department. We certify that counsel for the department has earned Rs. 1,000 as his fee. He is given six weeks' time to file a certificate. Costs awarded by this order will include costs of all the hearings including those entailed by the assessee's application for an order to the Commissioner that a reference be made. The

assessee's costs shall be taxed according to the certificate filed by counsel.

Let a copy of our judgment be sent to the Commissioner of Income Tax making the reference.

Order accordingly.

[IN THE CALCUTTA HIGH COURT.]

RAMJIDAS MAHALIRAM, *In re.*

McNair, J.

March 6, 1935.

INCOME TAX—RE-ASSESSMENT—JURISDICTION OF INCOME TAX AUTHORITIES—ESCAPE OF INCOME FROM ASSESSMENT IN FACT, NECESSITY OF—INITIATION OF PROCEEDINGS ON MERE SUSPICION THAT INCOME HAS ESCAPED—LEGALITY—ILLEGAL INITIATION OF PROCEEDINGS—POWER OF SINGLE JUDGE OF HIGH COURT TO ISSUE WRIT OF CERTIORARI—WRIT, WHEN GRANTED—INCOME TAX ACT (XI OF 1922), SECTION 34—GOVERNMENT OF INDIA ACT, 1915, SECTION 106 (2).

The assessees submitted a return of income for the year ending March 31, 1933, stating that they had sustained a loss of over 8 lakhs. The Income Tax Officer accordingly assessed them at 'nil' on December 23, 1933. On February 8, 1934, he, however, issued notice to the assessees under Section 34 of the Income Tax Act, stating that he had reason to believe that the assessees' income had wholly escaped assessment and calling upon the assessees to make a fresh return of income from all sources, which was assessable in the year ending March 31, 1933. The assessees submitted under protest a fresh return showing the same figures, and applied to the Commissioner under Section 33 to revise the Income Tax Officer's proceedings. The Commissioner refused to interfere either under Section 33 or Section 66 as the proceedings before the Income Tax Officer were still pending. The assessees thereupon applied to the High Court, on its original side, praying, inter alia, *for a writ of* certiorari *for quashing the proceedings of the Income Tax Officer under Section 34 and the subsequent proceedings :*

Held, (*i*) *that the High Court has power in a proper case to compel an Income Tax Officer to carry out a duty imposed upon him notwithstanding the provisions of Section 106 (2) of the Government of India Act, 1915, which provides that the High Court may not exercise any original jurisdiction in matters concerning revenue;*

(ii) that an application of this nature, not being an application for a reference under the Income Tax Act, could properly be heard by a single Judge of the High Court sitting on the original

(iii) that unless some item of income has in fact escaped taxation an Income Tax Officer has no power to initiate proceedings under Section 34 and his proceedings will be void and without jurisdiction if in fact no item of income had escaped assessment; he cannot act under Section 34 merely because he suspects or 'has reason to believe' that income has escaped assessment;

(iv) further, an Income Tax Officer cannot give himself jurisdiction by an erroneous finding of fact that income had escaped; it is not for him to decide whether the preliminary state of facts investing him with jurisdiction exists, that is, whether income has in fact escaped assessment;

(v) that, as the Act has provided the Commissioner with power to revise under Section 33 and the Commissioner had made an order under that section the assessees were not without a remedy against the order of the Income Tax Officer, and inasmuch as under the amended Income Tax Act the assessees were entitled to apply under Section 66 against an order under Section 33 prejudicial to them, they were not without a remedy against the Commissioner's order, and further as the order did not violate any rule of fundamental justice the present case was not one in which a writ of certiorari *should be issued.*

Cases referred to:

ALCOCK ASHDOWN & CO., LTD. *v.* CHIEF REVENUE AUTHORITY [1923] (50 I.A. 227; 47 Bom. 742; 75 I.C. 392; A.I.R. 1923 P.C. 138; 28 C.W.N. 762; 25 Bom. L. R. 920).

BURN & CO., *In re* [1934] (2 I.T.R. 30; 61 Cal. 132).

CHETTIAR FIRM, V.E.A. *v.* COMMISSIONER OF INCOME TAX, BURMA [1929] (7 Rang. 581; 3 I.T.C. 436).

COMMISSIONER OF INCOME TAX, BURMA *v.* C. P. L. E. CHETTIYAR FIRM [1934] (2 I.T.R. 201; 12 Rang. 322).

COMMISSIONER OF INCOME TAX, BURMA *v.* U. LU NYO [1933] (1 I.T.R. 373; 12 Rang. 118).

DEATH, *ex parte* [1852] (18 Q.B. 647; 118 E.R. 244).

KING *v.* BRADFORD [1908] (1 K.B. 365).

KING *v.* GENERAL COMMISSIONERS OF TAXES FOR CLERKENWELL [1901] (2 K.B. 879).

KING *v.* COMMISSIONERS FOR KENSINGTON [1913] (3 K. B. 370).

KING *v.* NORTH, *Ex parte* OAKLEY [1927] (1 K. B. 491).

LACHHIRAM BASANTLAL, *In re* [1930] (58 Cal. 909).

NATIONAL CARBON CO., *In re* [1934] (61 Cal. 450).

PARTINGTON *v.* ATTORNEY-GENERAL [1869] (L. R. 4 H. L. 100).

RAJENDRA NATH *v.* COMMISSIONER OF INCOME TAX, BENGAL [1934] (2 I. T. R. 71 ; 61 Cal. 285 ; 61 I. A. 10 ; 38 C. W. N. 814).

SATYENDRAMOHAN CHOWDHURY, *In re* [1930] (I.L.R. 58. Cal. 326 ; 4 I. T. C. 447 ; 129 I. C. 405).

SPOONER *v.* JUDDOW [1850] (4 M. I. A. 353).

TATA HYDRO-ELECTRIC AGENCY *v.* COMMISSIONER OF INCOME TAX, BOMBAY [1934] (2 I. T. R. 103 ; 58 Bom. 361).

THE QUEEN *v.* BOLTON [1841] (1 Q. B. 66 ; 113 E. R. 1054).

THE QUEEN *v.* COMMISSIONERS FOR THE SPECIAL PURPOSES OF INCOME TAX [1888] (21 Q. B. D. 313).

THE QUEEN *v.* NUNNELY [1858] (120 E. R. 728).

WHITE *v.* STEELE [1862] (12 C.B.N.S. 383 ; 142 E. R. 1191).

Application for a writ of *certiorari.*

Barwell, Claogh and *Jyoti P. Mitter*, for the applicants.

Roy (Advocate-General) and *Issacs*, for the Commissioner of Income Tax, Bengal.

MCNAIR, J.—This is an application on behalf of the firm of Mahaliram Ramjidas for a writ of *certiorari* directing the Commissioner of Income Tax, Bengal, to bring up the records of certain assessment proceedings pending before the Income Tax Officer of District IV-3, Calcutta, relating to an assessment in respect of the financial year 1932-33, wherein the registered partnership firm of Mahaliram Ramjidas are the assessees, to the end that an order of the said Income Tax Officer passed in the said proceedings on the 5th February, 1934, purporting to be under Section 34 of the Indian Income Tax Act, 1922, and all proceedings consequent upon such order be quashed, including an order of the Income Tax Commissioner, dated the 3rd of November, 1934, and purporting to dispose of an application by the assessees under Section 33 of the Act, dated the 15th September, 1934, or for such further or other orders by writ of prohibition or otherwise as the

Court may deem just and expedient. In the alternative, the applicants ask (i) for an order directed to the Commissioner of Income Tax, Bengal, requiring him to hear and determine the assessee's application of the 15th September, 1934, and/or to state a case, according to law, and (ii) for an injunction restraining the Income Tax Officer and/or the Commissioner from further proceeding under any order purporting to be under Section 34 of the Income Tax Act in regard to the assessees' income for the Sambat year 1987-88 pending the disposal of this motion.

The petitioners are a registered partnership carrying on business in Calcutta and use the Sambat year for accounting in the usual course of their business.

The Sambat year 1987-88 corresponds to the period from the 31st October, 1930, to the 9th of November, 1931.

Their income during the Sambat year 1987-88, for the purpose of income tax, fell to be assessed during the financial year ending on the 31st of March, 1933.

The return which was submitted by the petitioners contained a statement that the firm sustained a loss of over Rs. 8 lakhs.

The Income Tax Officer, on the 23rd December, 1933, made an assessment pursuant to Section 23 (3) of the Income Tax Act assessing the petitioners' firm at "nil".

On the 5th of February, 1934, the Income Tax Officer made an order for notice to issue under Section 22 (2) read with Section 34 of the Income Tax Act calling for a return of income assessable in 1932-33. The notice which was dated the 8th of February, 1934, stated that the Income Tax Officer had reason to believe that the assessees' income had wholly escaped assessment and he called upon the petitioners within thirty days of the receipt of the notice to deliver to him a return, in the attached form, of their income from all sources assessable in the year ending 31st of March, 1933.

Under protest, the petitioners made another return, wherein the figures shown corresponded with their former return for this period and the Income Tax Officer on the 21st of May, 1934, called for the petitioners' trading books for their accounting years 1987-88, 1985-86, and 1984-85. A further notice called for the petitioners' pass books for the years 1984-85 to 1988-89 a period of five years which was clearly in excess of the Income Tax Officer's powers. The petitioners were also required to give evidence. They appeared under protest in June, July and August,

1934, and produced their books. In August 1934, the petitioners wrote to the Income Tax Officer protesting against certain entries which had been recorded in the Income Tax Officer's books and which they characterised as being "erroneous."

On the 1st of September, 1934, the Income Tax Officer wrote to the petitioners saying that he had held that all the proceedings relating to their assessment were valid, and that they should be continued and computed. For this purpose the accounts for the Sambat year 1987-88 would be "thoroughly examined," as well as the books already called for. The petitioners state that they asked for particulars of the reasons for the Income Tax Officer's procedure, which they contended were *ultra vires*, and for the orders on which they were based, but without result.

On the 15th of September, 1934, they presented a petition to the Commissioner of Income Tax under, amongst others, Section 33 of Income Tax Act.

The Commissioner, on the 8th of December, 1934, forwarded to the petitioners a copy of his order dated the 3rd of November, 1934, which was in the following terms:—

"Order:—I have considered the application of the assessees, dated the 15th of September, 1934. I am not prepared to interfere or to take any action under Section 33 or 66 of the Act, at this stage, when the assessment is still before the Income Tax Officer. The assessees may be informed accordingly."

The petitioners complained that this method of disposing of this matter was to pass an order prejudicial to the petitioners and they submitted that the Commissioner's action was without jurisdiction. They submit that the machinery of the Act, does not give them any method of obtaining relief, and they accordingly applied to this Court for the issue of a writ of *certiorari* addressed to the Commissioner, to have the proceedings quashed. In the alternative, they asked for an order under Section 45 of the Specific Relief Act, 1877, requiring the Commissioner to hear the complaint or to state a case. During his reply Mr. Barwell for the petitioners stated that the only relief for which he was now asking in view of the arguments for the Crown and the affidavit of the Commissioner, was for a writ of prohibition.

At the outset of the hearing, the Advocate-General, who appeared to oppose the application, submitted a preliminary objection to the effect that the application as framed would not lie. He

referred to paragraph 24 of the petition, in which it is stated that under Section 66 of the Income Tax Act an assessee cannot compel an Income Tax Commissioner to state a case except in reference to orders under Section 31 or 32, which do not apply here, and to their contention that in the circumstances they were faced with a complete denial of justice. He relies on the amendment of Section 66 of the Income Tax Act (XI of 1922) which was made by Act XVIII of 1933. Prior to the amendment, Section 66, sub-section (2) read as follows :—

"Within sixty days of the date on which he is served with notice of an order under Section 31 or Section 32...assessee in respect of whom the order......was passed may, by application accompanied by a fee of one hundred rupees or such lesser sum as may be prescribed, require the Commissioner to refer to the High Court any question of law arising out of such order...and the Commissioner shall, within sixty days of the receipt of such application draw up a statement of the case and refer it with his own opinion thereon, to the High Court."

The Act has been amended in 1933 by adding after the words "Section 32" the following words "or of an order under Section 33 enhancing an assessment or otherwise prejudicial to him" so that the section now reads :—

"Within sixty days of the date on which he is served with notice of an order under Section 31 or Section 32 or of an order under Section 33 enhancing an assessment or otherwise prejudicial to him......the assessee......may......require the Commissioner to refer to the High Court any question of law arising out of such order......"

Sections 31 and 32 which deal with an appeal to the Assistant Commissioner and from him to the Commissioner are admittedly irrelevant to the present matter.

Section 33 empowers the Commissioner to call for the record of any proceeding, to make enquiries and pass such orders as he thinks fit, provided that he shall not pass any order prejudicial to an assessee without hearing him or giving him a reasonable opportunity of being heard.

The petitioners in paragraph 24 of their petition state that they are unable to obtain a reference except in regard to orders made under Section 31 or 32 from which it would appear that they were unaware of the recent amendment.

Section 66, sub-Section (2), now provides that within sixty days of the date on which he is served with notice of an order under Section 33 enhancing an assessment or otherwise prejudicial to him an assessee may by application accompanied by a fee of one hundred rupees or such lesser sum as may be prescribed, require the Commissioner to refer to the High Court any question of law arising out of such order and the Commissioner, shall, within sixty days, state a case and refer it to the High Court.

There follow two provisos. The first, that a reference shall lie from an order under Section 33 only on a question of law arising out of that order itself, and not on a question of law arising out of a previous order under Section 31 or Section 32, revised by the order under Section 33.

The second, that, if in exercise of his power of revision under Section 33, the Commissioner decides the question or rejects the application, or refuses to state the case, the assessee may, within thirty days from the date on which he receives notice of the order passed by the Commissioner, withdraw his application and obtain a refund of his fee.

Sub-Section (3) provides that if an application be made under sub-Section (2) and the Commissioner refuses to state the case on the ground that no question of law arises, the assessee may apply to the High Court, and the High Court may require the Commissioner to state the case and refer it to the Court.

The Advocate-General contends that the recent amendment of the Income Tax Act, by Act XVIII of 1933, has given an assessee remedies which he did not previously possess; that he has not chosen to avail himself of those remedies, and that he cannot now say that there is no machinery within the terms of the Act whereby he can obtain relief. In the circumstances, he says, the petitioners have not shown that they are entitled to invoke those powers of the Court which are only applicable to exceptional circumstances.

It is further argued that the Commissioner has not come to any decision. He has not passed an order but has made a statement that in his opinion the time is not yet ripe for him to interfere with the proceedings which are being conducted by the Income Tax Officer.

The communication by the Commissioner, dated the 3rd of November, 1934, is headed "order" and it must be taken to have

been intended to be an " order ". It purports to have been made after considering the assessees' application that the Commissioner should exercise his discretion under Section 33 and it must be assumed that it is an order made in the exercise of that discretion and under the powers provided by Section 33. It follows that if it is an order prejudicial to the assessees and containing a question of law, Section 66 provides machinery whereby the assessees may have the legality of that order referred to the High Court for decision.

The assessees, in support of their contention that they are not confined to the relief afforded by the provisions of the Income Tax Act, rely on the case of *Alcock, Ashdown and Company, Limited* v. *Chief Revenue Authority of Bombay*, where the Privy Council held that when power is given to a public authority there may be circumstances which will couple the power with the duty to exercise it, and that under the provisions of Section 51 of the old Income Tax Act of 1918 "always supposing that there is a serious point of law to be considered, there does lie a duty upon the Chief Revenue authority to state a case for the opinion of the Court, and if he did not appreciate that there is such a serious point, it is in the power of the Court to control him and to order him to state a case ". Since the enactment of the new Income Tax Act of 1922 the above case has to some extent become obsolete.

The new Act has in Section 66 empowered the Court to require the Commissioner to state a case and refer it and has laid down the limitations under which such a reference shall be made.

There is in the framework of the Act itself machinery, by which the assessee may bring the matter before the Court and he can no longer contend that the Act provides no specific or adequate remedy. See *V.E.A. Chettyar Firm* v. *Commissioner of Income Tax*, *The Commissioner of Income Tax, Burma* v. *C.P.L.E. Firm* and *Tata Hydro-Electric Agency, Limited* v. *Commissioner of Income Tax, Bombay*.

This objection is in my opinion valid. I will deal with it more fully in regard to the claim for a writ of prohibition at the conclusion of my judgment.

The next contention of the Advocate-General is that there is no power in the High Court to issue a writ against the Income Tax Commissioner. He refers to Clause 4 of the Charter establishing the Supreme Court at Fort William in Bengal. By that clause,

the Chief Justice and Puisne Justices are to have such jurisdiction and authority as the Justices of the Court of King's Bench have, and may lawfully exercise within that part of Great Britain called England, by the common law thereof. By Clause 21 of the Charter it was ordained and established that all Courts and Magistrates therein referred to should "be subject to the order and control of the said Supreme Court of Judicature at Fort William in Bengal, in such sort, manner and form, as the inferior Courts and Magistrates of......England are, by law, subject to the order and control of our Court of King's Bench, to which end, the said Supreme Court of Judicature, at "Fort William in Bengal," was "empowered and authorised, to award and issue a writ or writs of mandamus, *certiorari*, *procedendo* or error....................directed to such Courts or Magistrates as the case may require, and to punish any contempt of a wilful disobedience thereunto by fine and imprisonment".

In 1780 the East India Company Act, 1780 (21 Geo. III c. 70), was enacted. Section 8 of that Act provided that the Supreme Court shall not have or exercise any jurisdiction, in any matter concerning the revenue or concerning any act ordered or done in the collection thereof, according to the usage and practice of the country or the regulations of the Governor-General in Council.

The Government of India Act (5 & 6 Geo. V c. 61) which repealed the above Act, provided by Section 106, sub-section (2) that the High Courts have not and may not exercise any original jurisdiction in any matter concerning the revenue, or concerning any act ordered or done in the collection thereof according to the usage and practice of the country or the law for the time being in force.

The contention is that in matters of revenue the High Court has no jurisdiction, and that income tax being a matter concerning revenue or its collection, the High Court may not exercise its powers against the Income Tax Commissioner.

This argument was put forward on behalf of the Crown in the case to which I have already referred, *Alcock, Ashdown and Company, Limited* v. *Chief Revenue Authority of Bombay*, but the Privy Council held that the High Court had power to make an order requiring the Chief Revenue Authority to perform a duty under the Income Tax Act. It is noteworthy, however, that the aid of the Court was there invoked under Section 46 of the Specific Relief Act which enables the High Court to make an order

requiring any Specific Act to be done or forborne......by any person holding a public office whether of a permanent or a temporary- nature.........subject to certain provisos which are cumulative.

A question in the appeal was whether the Court had any jurisdiction to order the Chief Revenue Authority to state a case, and from the report it appears, that, before the Board, it was argued " that even if the Authority had a duty, the Court could not require him to exercise it"; and for this purpose reliance was placed upon the well-known general purview of Indian legislation which excludes matters of revenue from the consideration of the ordinary Civil Courts, the principle being exemplified in the case of *Spooner* v *Juddow*, and upon Section 106, sub-section (2) of the Government of India Act". LORD PHILLIMORE in delivering the opinion of the Board says [I.L.R. 47 Bom. 742 at 749] :—

" Upon the point thus broadly stated, their Lordships have no difficulty in pronouncing a decision. To argue that if the legislature says that a public officer, even a Revenue Officer, shall do a thing, and he without cause or justification refuses to do that thing, yet the Specific Relief Act would not be applicable, and there would be no power in the Court to compel him to give relief to the subject, is to state a proposition to which their Lordships must refuse assent......In their Lordships' view, the order of a High Court to a Revenue Officer to do his statutory duty would not be the exercise of " original jurisdiction in any matter concerning the revenue."

Although, as I have stated above, the material part of that decision can no longer be relied on owing to the amendment of the Income Tax Act, there is no reason to doubt the validity of the general proposition there laid down that this Court has power in a proper case to compel a public officer, and even a revenue officer, to carry out a duty imposed upon him.

The learned Advocate-General took a further preliminary objection that a single Judge on the Original Side is not competent to deal with an application of this character. It should be made, he says, before a Bench of at least two Judges of the High Court and that Bench should be the Bench appointed by the Chief Justice to deal with income tax matters.

In this connection reliance is placed, first, on Section 66-A, sub-section (1), of the Income Tax Act which provides that when

any case has been referred to the High Court under Section 66, it shall be heard by a Bench of not less than two Judges of the High Court; secondly, on the rules made under the Income Tax Act which are set out in Chapter XXX-A of the Rules and Orders of the Calcutta High Court (Original Side).

Rule 1 provides that all references under Section 66 of the Indian Income Tax Act, 1922,......shall be presented to the Registrar, Original Side, and shall be dealt with on the Original Side.

Rule 3 provides that the Registrar shall lay the matter before the Chief Justice who shall appoint a Bench under Section 66-A of the Income Tax Act to hear the reference.

Rule 5 provides that every application under Section 66 (3) of the said Act shall be presented to the Registrar, Original Side, who shall submit the same to the Chief Justice or to the Bench appointed by the Chief Justice.

Rule 6 is also relied on, which provides that vakils and attorneys shall be entitled to appear and act in all matters governed by these rules.

With reference to Rule 6 it has been argued by the Advocate-General that while vakils and attorneys can appear in income tax matters, in matters on the Original Side, only those counsel or advocates who have been specially admitted are entitled to appear and plead.

This is not a reference, nor is it an application under the Income Tax Act, and neither that Act nor the rules under it are applicable.

Although, incidentally, the matter concerns income tax, and the provisions of the Income Tax Act have to be considered in coming to a decision, yet this is not an application under Section 66 or any other section of the Income Tax Act. The relief sought is by a writ of *certiorari* or prohibition which is issued by the Court under the power and authority conferred on it by the Charter.

I have already referred to those powers and it was recently decided in *In re National Carbon Company, Incorporated*, that those powers include the power in a proper case to issue a writ of prohibition.

It was there pointed out, that there is, in the Charter, no mention of any authority to issue a writ of prohibition, but PANCKRIDGE, J., sitting on the Original Side of this Court, held in a decision with which I am fully in accord, that there was no intention by Clause 21 of the Charter to curtail the powers, co-extensive with those of the King's Bench, which had been given by Clause 4 and which include the power to issue a writ of prohibition.

In was never suggested, and I do not think it can be suggested, that a Judge sitting on the Original Side has not the right to exercise the powers with which the Court is vested under the Charter and those are the powers which are now invoked.

Assuming then that the facts are such as to justify the issue of a writ as prayed, I am of opinion that the application was rightly made on the Original Side of the Court, even though the subject-matter of the application be connected with proceedings under the Income Tax Act.

These were the preliminary questions argued. On the merits Mr. Barwell submits that the order of the Income Tax Officer of the 5th of February, 1934, is without jurisdiction.

The assessees made their return on the 21st of December 1932 and forwarded it without profit and loss account to the Income Tax Officer, who served a notice under Section 22 (4) on the proprietors of the firm to produce their books.

The assessment order shows that Mr. Kantilal Jatia, a member of the firm, appeared in response to the notice and produced the firm's *rakarah*, *nakal* and *khata* and explained the items.

On 23rd of December, 1932, the firm was assessed under Section 23 (3) at "Nil" for 1932-33, and an application under Section 26 A to renew the firm's registration for the purposes of the Act was granted.

On the 5th of February 1934, the Income Tax Officer made the order for a notice to issue under Section 22 (2) read with Section 34 and on the 8th of February 1934, the following notice was received by petitioners:—

"Notice under Section 34 of the Income Tax Act (XI of 1922) Office of the Income Tax Officer, District IV-3, Calcutta. Dated Calcutta, the 8th February, 1934. No. 1288/IV-3. The proprietors Mahaliram Ramjidas (firm), 21, Roopchand Ray Street, Calcutta

Whereas I have reason to believe that your income from business and other sources which should have been assessed in the financial year ending 31st March, 1933, has wholly escaped assessment, I therefore propose to assess the said income that has escaped assessment.

I hereby require you to deliver to me, not later than 9th March, 1934, within 30 days of the receipt of this notice a return in the attached form of your income from all sources which was assessable in the said year ending 31st March, 1933. Sd....7-2-34."

Section 34 provides:—

"If for any reason income, profits or gains chargeable to income tax has escaped assessment in any year or has been assessed at too low a rate, the Income Tax Officer may, at any time within one year of the end of that year, serve on the person liable to pay tax on such income, profits or gains..............a notice containing all or any of the requirements which may be included in a notice under sub-section (2) of Section 22, and may proceed to assess or re-assess such income, profits or gains, and the provisions of this Act shall, so far as may be, apply accordingly as if the notice were a notice issued under that sub-section."

The section provides for a re-opening of the assessment and empowers the income tax authorities to call for books and evidence, but before these powers may be exercised and the assessment that has been closed may be re-opened the essential pre-requisite is that something chargeable to income tax has escaped assessment. The notice under Section 34, it will be observed, merely states that the income tax authority "has reason to believe" that income has escaped assessment. That Mr. Barwell contends, is not sufficient. The Act in many instances, notably in Sections 22 (2), 23 (1) and (2), 23A, 24A, 25, 46 (1) and elsewhere uses expressions such as "in the Income Tax Officer's opinion", "If the Income Tax Officer is satisfied" or "If the Income Tax Officer has reason to believe" or "the Income Tax Officer may in his discretion direct," which give the Income Tax Officer a discretion and power to use that discretion.

In Section 34 no such discretion is allowed. What is contemplated is that some item liable to tax has in fact escaped taxation, and only when that fact is in existence may the income tax authorities use their powers to reopen an assessment which has already been closed and which under the scheme of the Act is otherwise intended under Section 23 to be closed finally.

It is the general policy of the law that when accounts have been gone into and a balance has been struck and agreed upon, such an agreement should not lightly be set aside. It is not unlikely that the legislature had this principle in mind and were unwilling to have an assessment re-opened merely at the discretion of the income tax authority in view of the inevitable dislocation to the assessee's accounts and business.

In any event, Section 34 has been so worded that it does not leave the matter in the discretion of the Income Tax Officer but provides that the machinery in Section 22 may be set in motion a second time only if an item chargeable to income tax has escaped assessment, and the ordinary meaning of those words is that the escape from assessment is a fact.

Moreover, that is a fiscal statute in which the actual words of the Act must be strictly adhered to. See *Partington* v. *The Attorney-General.*

It is contended that even if the order had stated, "whereas your income which should have been assessed has wholly escaped assessment" that statement would have been untrue and no valid order or proceedings, could be made or held, founded on an incorrect premise.

An assessment has been made and it cannot be said with truth that the assessee's income from all sources has wholly escaped assessment.

In *In re Lachhiram Basantlal*, RANKIN, C.J., in delivering the judgment of the Court said :—

"Section 34 deals with income which has escaped assessment and it may be, though it is not necessary for the present purpose to decide it, that income cannot be said to have escaped assessment except in the case where an assessment has been made which does not include the income."

And in *Rajendranath Mukerji* v. *Commissioner of Income Tax, Bengal*, LORD MACMILLAN says :—

"The fact that Section 34 requires a notice to be served calling for a return of income which has escaped assessment strongly suggests that income which has already been duly returned for assessment, cannot be said to have "escaped" assessment within the statutory meaning.

In *In re Satyendramohan Roy Chaudhuri*, the question for decision was whether, after an assessment made under Section 23(4) of the Act is reopened under Section 34, by reason of certain specified heads of income having been assessed at too low a figure, the whole assessment may be reopened at the option of the assessee, so that his income under one head should be reduced, if his income under another head were enhanced.

The Commissioner of Income Tax was of opinion that Section 34:

"gives no general powers of revision to the Income Tax Officer and that the Income Tax Officer cannot reopen the assessment of the income, profits or gains of an assessee from any source in respect of which he has no reason to believe that the assessee has been under-assessed. In his view, it appears to be the intention of the Act that general powers of revision should only be exercised by the Commissioner acting under Section 33 and that the powers of the Income Tax Officer under Sections 34 and 35 are strictly limited by the terms of the sections themselves."

It was held that the assessee had no right to have the whole assessment reopened.

In delivering judgment the learned Chief Justice says:—

" As a matter of the true construction of this section, it appears to me that if the legislature had meant to say that if in any case it appears to the Income Tax Officer that an assessee has been assessed upon too low a figure or too low a rate the Income Tax Officer may issue a fresh notice under Section 22 (2) and may proceed to reassess such assessee afresh, the language employed would have been noticeably different from that which we find in the present section."

In some of the cases to which I have been referred, the Income Tax Officer has stated the particular heads of income which have escaped assessment; in others it is not clear what form of notice was issued. There is no standard form of notice. See *In re Burn & Co.*

But apart from the fact whether the notice was correct in form, the principle which the above cases lay down is that the words of the Act do not empower the Income Tax Officer to reopen an assessment merely to enquire further into the assessees' books in case something assessable may be found : and if I am right in my view, that it is an essential pre-requisite to reopening an

assessment that an item of income, profits or gains has escaped assessment, the Income Tax Officer cannot give himself jurisdiction by an erroneous finding of fact. The assessees complain that they have never been given any indication of the heads of income which are said to have escaped assessment and no reply has been received to their request for information. If the Income Tax Officer is entitled to reopen an assessment merely on suspicion, no doubt he is justified in maintaining silence, but in my view no such intention of the legislature appears in the words of the section. This view is supported by the decision of a Bench of the Burma High Court in *Commissioner of Income Tax* v. *U Lu Nyo*, where it was held that when one Income Tax Officer had completed an assessment an attempt by his successor to go behind and revise the assessment merely because he disagreed with his predecessor's finding as to the amount of assessable income was not an assessment under Section 34.

Mr. Issacs, who in its later stages argued the case for the Crown in the absence of the Advocate-General, contended that the jurisdiction of the Income Tax Officer was territorial, and provided the assessee was within his territorial jurisdiction, which was not contested, the Income Tax Officer was empowered to perform the function entrusted to him under Section 22 and Section 34 and for that purpose to come to a finding of fact. I cannot agree that the mere grant of territorial jurisdiction entitles the Income Tax Officer to come to a finding of fact enabling him to reopen an assessment under Section 34. The real question in my opinion is whether the section is so worded as to grant the Income Tax Officer apart from his territorial jurisdiction, the power to determine conclusively the question of fact upon which his jurisdiction depends.

The legislature, in my view, has provided that if a certain state of facts exists and is shown to the Income Tax Officer to exist, before he proceeds to reopen the assessment under Section 34, he shall have jurisdiction to take proceedings, but not otherwise.

It is not for him to decide whether that state of facts exists, and if he reopens the assessment without its existence he is acting without jurisdiction.

I find no words in Section 34 which empower the Income Tax Officer to determine whether the preliminary state of facts exists.

In this connection I have been referred to the cases of *The Queen* v. *Bolton*; *The Queen* v. *Nunneley* and *The Queen* v. *Commissioners for Special Purposes of Income Tax*, in which LORD ESHER, M. R., states the two contentions and points out that the correctness of the one or the other must depend on the powers with which the legislature has invested a tribunal or body. See *The King* v. *General Commissioners of Taxes for the District of Clerkenwell* and *The King* v. *Bradford*.

Mr. Isaacs further argued that prohibition could only issue with reference to persons exercising judicial functions and that the functions of the Income Tax Officer are administrative.

In support of this argument he referred to the cases of *Ex parte Death* and *The King* v. *The Commissioners for the General Purposes of Income Tax for Kensington*.

But these cases which are decided on the English Income Tax Acts are not authoritative on a construction of the Indian Act where the Income Tax Officer combines the duties under the English Acts of the Surveyor, the Commissioner and the Special Commissioners. In India, for instance, the assessee may be called upon under Section 23 to give evidence at the outset, in support of his return, whereas the Surveyor in England has no right to obtain legal evidence and is merely an administrative Officer.

The Commissioner's jurisdiction does not begin until the Surveyor has discovered an omission under Section 52 of the Taxes Management Act but the Income Tax Officer in India is vested at the outset with judicial powers and Section 37, which invests the Income Tax Officer with power to issue commissions for the examination of witnesses, provides that any proceeding before an Income Tax Officer.........under "this chapter" shall be deemed to be a "judicial proceeding". "This Chapter" includes the provisions of Sections 22 and 34.

At the conclusion of their case the petitioners contended that their real grievance was against the orders of the Income Tax Officer under Section 22 and Section 34 which were without jurisdiction and for which the Act gives no specific or adequate remedy. The answer is that the Act does provide the Commissioner with power of revision under Section 33 and the Commissioner has purported to exercise those powers under Section 33 and has made an order.

The petitioners allege that that order is unsatisfactory and that the Commissioner has given them no opportunity of being heard. If that be so the question raised is a question on the construction of the Act and so a question of law, and as it is an order which the assessees consider prejudicial to them, they could have availed themselves of the provisions of Section 66 and had the legality of the order tested by the Court. Their contention that an application under Section 66 would entail delay and that delay is the essence of their complaint, even if correct, does not justify them in neglecting the remedy provided by the Act, and in seeking instead to call in aid the extraordinary powers of the Court.

It is evident that the legislature intended the Commissioner to deal with questions that came to his notice under Section 33, and if he passed an order which the assessees considered prejudicial it provided a method by which the legality of the proceedings could be tested. It was obviously their intention that the provisions of Section 66 relating to a reference should be strictly complied with, and, if there was no such compliance, they intended the Commissioner's orders to be final and the jurisdiction of the High Court to be excluded.

It is clear from the English decisions that the power of exercising prohibition is discretionary, and that the Court should not be chary of exercising it to control persons who are entrusted with the power of imposing any obligation upon individuals and who attempt to exercise those powers in excess of their jurisdiction.

It has also been laid down that the fact that there is a right of appeal is not necessarily fatal to a claim for prohibition: *White* v. *Steele* approved in *The King* v. *North, Ex parte Oakley*, but the guiding principle appears to be that the writ in such a case will not issue unless the want of jurisdiction complained of is based upon a breach of a fundamental principle of justice.

Here the orders complained of do not, in my opinion, come within the exception and I am not satisfied that this is a case in which a writ of prohibition should issue.

The Commissioner stated in his order of the 3rd of November, 1934, that he was not willing, at the date, to interfere or take any action under Section 33 or Section 66 of the Act. In view of my decision that the proceedings by the Income Tax Officer in

revision were irregular, the learned Commissioner may feel called upon now to look further into the matter.

The facts have been stated on affidavit by the petitioners and complaints are made of the actions of the Income Tax Officer. The only affidavit in opposition is by the Commissioner who must of necessity state matters according to the information he has received. No affidavit is filed by the Income Tax Officer.

After careful consideration of all the circumstances I order that the application be dismissed but that each party do bear their own costs.

Application dismissed.

Solicitors :—*Panna Lale De*, for the applicants ; *Government Solicitor*, for the Commissioner of Income Tax, Bengal.

[IN THE PRIVY COUNCIL.]

NATIONAL MUTUAL LIFE ASSOCIATION OF AUSTRALASIA, LTD.

v.

COMMISSIONER OF INCOME TAX, BOMBAY PRESIDENCY AND ADEN.

Lord Thankerton, Sir Lancelot Sanderson and Sir George Rankin.

November 18, 1935.

INCOME TAX—FOREIGN COMPANY—ASSESSMENT OF INCOME OF INDIAN BUSINESS—PROPER METHOD—REVENUE ACCOUNT AND BALANCE SHEET, WHETHER RELIABLE DATA—APPLICATION OF RULE 35, WHEN JUSTIFIABLE—MUTUAL INSURANCE COMPANY—CALCULATION OF INCOME—EXCLUSION OF INCOME FROM PARTICIPATING POLICIES—INDIAN INCOME TAX ACT (XI OF 1922), SECTIONS 13 AND 22 (1)—INCOME TAX RULES, RULE 35.

The Income Tax Officer is only authorised to have recourse to the method of computation provided by Rule 35 of the Income Tax Rules " in the absence of more reliable data'' and this requires (a) a scrutiny of the data which in fact had been made available to the Income Tax Officer, irrespective of any question as to the validity or correctness of the return made under Section 22 (1) of the Income Tax Act, and (b) a consideration of the reliability of those data for the purpose of the proper computation of the income, profits or gains of the company in accordance with Section 13 of the Act.

The assessee was a mutual life insurance company with its head office at Australia and a branch in British India at Bombay. It made a return of its total income from its business in India for the year ending September 30, 1930 at £3,241-14-8 and along with the return submitted a revenue account and balance-sheet for that year. The triennial valuation report of the whole business for the triennial period ending on September 30, 1928 and the balance sheet and revenue account of the entire business for the year of account, in both of which the average rate of interest earned by the invested funds of the company appeared, were also produced. The Income Tax Officer held that the data supplied by the company were not more reliable

than the method prescribed in Rule 35 of the Income Tax Rules and assessed the income under Rule 35. He found that the premium income of the company as a whole for the year in question was £3,244,476, and that the premium income of the company in British India for the same period was £87,942. The net assessable profit of the company as a whole based on the triennial investigation was £1,405,027 and accordingly he assessed the taxable income in India at the proportionate profit in British India, namely, £38,083. The questions being whether the Income Tax Officer was justified in law in applying Rule 35 and whether the assessment was legal:

Held, (*1*) *that the Income Tax Officer was entitled to take the view that the income of the Indian business could not be properly deduced from the data supplied by the company and that the information submitted by the company did not afford more reliable data for computation of the income of the Indian business than the method prescribed by Rule 35* (*which is based on the total income, profits or gains of the company, the proportion attributable to the Indian business being calculated on the ratio of the Indian premium income to their total premium income*) *and the Income Tax Officer was justified in resorting to Rule 35. Computation on the basis of the triennial valuation reports is the most reliable method of computation in the case of life insurance companies. The interest earned on investments, though it is an element in the ascertainment of the income, profits or gains, is not by itself a reliable datum for such ascertainment.*

(*2*) *That the assessment made was not, however, a valid or legal assessment, inasmuch as the ' total income, profits or gains of the companies referred to in Rule 35 is the income, profits or gains* as they would be ascertained for the purposes of the Act *and even assuming that the 'premium income' referred to in Rule 35 includes premiums received in respect of participating policies, in calculating the nett assessable profit the principle of* Styles' case *had been altogether ignored.*

Commissioner of Income Tax, Bombay v. *National Mutual Life Association of Australasia, Ltd.* [*1933*] 1 I.T.R. 350 ; I.L.R. 55 Bom. 637 *reversed.*

New York Life Insurance Company *v.* Styles (1889) 14 A. C. 381 referred to.

Appeal against the judgment of the Bombay High Court in Reference No. 11 of 1932 dated February 27, 1933 reported in (1933) 1 I. T. R. page 350 and I. L. R. 55 Bom. 637.

A. M. Latter, K. C. and *C. L. King*, for the appellants.

A. M. Dunne, K. C. and *R. Hills*, for the respondent.

LORD THANKERTON—This is an appeal from a judgment of the High Court of Judicature at Bombay, dated February 27, 1933, whereby the Court answered adversely to the appellants two questions of law, which had been referred to the Court by the Commissioner of Income Tax, Bombay Presidency, on his own motion, under Section 66 (1) of the Indian Income Tax Act (XI of 1922).

The appellants are a mutual life insurance company, whose head office is in Melbourne, Australia. They have branches all over the world, and in India they have two branches one of which is in Bombay and the other in Calcutta. The questions of law arise out of a dispute as to the method of computation of the income, profits or gains of the appellant company in the business of its Indian branch offices for the purpose of its assessment to income tax for the financial year ending on March 31, 1932.

The facts are set out in the letter of reference and may be summarised as follows:—The company is limited by guarantee and has no share capital, the liability of each member being limited to the nominal sum of £1. Every person who insures his life with the company under a participating policy is deemed to have agreed to become a member of the company. There are no shareholders and all the surplus profit is divided amongst the members, who are the persons who take out participating policies. The company also does business in annuities, loans on the security of policies, etc.

Under Article 85 of the articles of association a triennial actuarial valuation is made by the actuary of the company for all its business, and the surplus profit for the three years thus ascertained is distributed amongst the participating policy-holders. As originally framed, this article provided for a separate valuation for each branch or class of the company's business, but this has now been altered and only a consolidated valuation report is drawn up including all the company's business. The

articles do not provide for a separate valuation of the business of branch offices, and it is not stated whether in fact such separate valuations have been made.

From the documents submitted along with the letter of reference it appears that approximately 98 per cent. of the company's total business is done with its members, the participating policyholders. Before the Board, it was accepted throughout by both parties that the principles laid down in the English case of *New York Life Insurance Co.* v *Styles* apply in India; this was decided by the High Court in a case between the parties to this appeal in 1931, *Commissioner of Income Tax, Bombay Presidency* v. *National Mutual Life Association of Australasia, Ltd.* and, while not meaning thereby to imply any doubts, their Lordships need not and do not express any opinion on this matter.

The following are the material provisions of the Indian Income Tax Act, 1922, and the statutory rules made thereunder:—

3. Where any Act of the Indian Legislature enacts that income tax shall be charged for any year at any rate or rates applicable to the total income of an assessee, tax at that rate or those rates shall be charged for that year in accordance with, and subject to the provisions of this Act in respect of all income, profits and gains of the previous year of every individual, Hindu undivided family, company, firm and other association of individuals.

4—(1) Save as hereinafter provided, this Act shall apply to all income, profits or gains, as described, or comprised in Section 6, from whatever source derived, accruing or arising or received in British India or deemed under the provisions of this Act to accrue or arise, or to be received in British India.

(2) Profits and gains of a business accruing or arising without British India to a person resident in British India shall, if they are received in or brought into British India, be deemed to have accrued or arisen in British India and to be profits and gains of the year in which they are so received or brought, notwithstanding the fact that they did not so accrue or arise in that year provided that they are so received or brought in within three years of the end of the year in which they accrued or arose.

10. (1) The tax shall be payable by an assessee under the head "business" in respect of the profits or gains of any business carried on by him.

13. Income, profits and gains shall be computed for the purposes of Sections 10, 11 and 12 in accordance with the method of accounting regularly employed by the assessee : Provided that, if no method of accounting has been regularly employed, or if the method employed is such that, in the opinion of the Income Tax Officer, the income, profits and gains cannot properly be deduced therefrom, then the computation shall be made upon such basis and in such manner as the Income Tax Officer may determine.

22. (1) The principal officer of every company shall prepare, and, on or before the fifteenth day of June in each year, furnish to the Income Tax Officer a return in the prescribed form and verified in the prescribed manner, of the total income of the company during the previous year: Provided that the Income Tax Officer may, in his discretion, extend the date for the delivery of the return in the case of any company or class of companies.

(4) The Income Tax Officer may serve on the principal Officer of any company or on any person upon whom a notice has been served under sub-Section (2) a notice requiring him, on a date to be therein specified, to produce or cause to be produced such accounts or documents as the Income Tax Officer may require: Provided that the Income Tax Officer shall not require the production of any accounts relating to a period more than three years prior to the previous year.

23. (1) If the Income Tax Officer is satisfied that a return made under Section 22 is correct and complete, he shall assess the total income of the assessee, and shall determine the sum payable by him on the basis of such return.

(2) If the Income Tax Officer has reason to believe that a return made under Section 22 is incorrect or incomplete he shall serve on the person who made the return a notice requiring him, on a date to be therein specified, either to attend at the Income Tax Officer's office or to produce, or to cause to be there produced, any evidence on which such person may rely in support of the return.

(3) On the day specified in the notice issued under sub-Section (2), or as soon afterwards as may be, the Income Tax

Officer, after hearing such evidence as such person may produce and such other evidence as the Income-Tax Officer may require, on specified points, shall, by an order in writing, assess the total income of the assessee, and determine the sum payable by him on the basis of such assessment.

(4) If the principal officer of any company or any other person fails to make a return under sub-Section (1) or sub-Section (2) of Section 22, as the case may be, or fails to comply with all the terms of a notice issued under sub-Section (4) of the same section or, having made a return, fails to comply with all the terms of a notice issued under sub-Section (2) of this section, the Income-Tax Officer shall make the assessment to the best of his judgment and, in the case of a registered firm, may cancel its registration.

Provided that the registration of a firm shall not be cancelled until fourteen days have elapsed from the issue of a notice by the Income Tax Officer to the firm intimating his intention to cancel its registration.

59. (1) The Central Board of Revenue may, subject to the control of the Governor-General in Council, make rules for carrying out the purposes of this Act and for the ascertainment and determination of any class of income. Such rules may be made for the whole of British India or for such part thereof as may be specified.

(2) Without prejudice to the generality of the foregoing power, such rules may—

(*a*) prescribe the manner in which, and the procedure by which, the income, profits and gains shall be arrived at in the case of :—

....

(*ii*) insurance companies;

(3) In cases coming under Clause (*a*) of sub-Section (2) where the income, profits and gains liable to tax cannot be definitely ascertained or can be ascertained only with an amount of trouble and expense to the assessee which, in the opinion of the Central Board of Revenue, is unreasonable, the rules made under the sub-section may—

(*a*) prescribe methods by which an estimate of such income, profits and gains may be made, and

(*b*) in cases coming under sub-Clause (*i*) of Clause (*a*) of sub-Section (2), prescribe the proportion of the income which shall be deemed to be income, profits and gains liable to tax,

and an assessment based on such estimate or proportion shall be deemed to be duly made in accordance with the provisions of this Act.

Rule 25.—In the case of life assurance companies incorporated in British India whose profits are periodically ascertained by actuarial valuation, the income, profits and gains of the life assurance business shall be the average annual net profits disclosed by the last preceding valuation, provided that any deductions made from the gross income in arriving at the actuarial valuation which are not admissible for the purpose of income tax assessment, and any Indian income tax deducted from or paid on income derived from investments before such income is received, shall be added to the net profits disclosed by the valuation.

Rule 26—Rule 25 shall apply also to the determination of the income, profits and gains derived from the annuity and capital redemption business of life assurance companies, the profits of which can be ascertained from the results of an actuarial valuation.

Rule 27.—If the Indian income tax deducted from interest on the investments of a company exceeds the tax on the income, profits and gains thus calculated, a refund may be permitted of the amount by which the deduction from interest on investments exceeds the tax payable on such income, profits and gains.

Rule 35.—The total income of the Indian branches of non-resident insurance companies (Life, Marine, Fire, Accident, Burglary, Fidelity Guarantee, etc.), in the absence of more reliable *data*, may be deemed to be the proportion of the total income, profits or gains of the companies, corresponding to the proportion which their Indian premium income bears to their total premium income."

On July 22, 1931, the appellant company made a return of its total income, profits or gains from its business in India, based on the year ending September 30, 1930, as the year of account, at a sum of £ 3,241 14s. 8d. Along with the return a revenue account and balance sheet for that year was submitted. In the course of meetings with the Income Tax Officer, certain

further information was submitted, which did not satisfy the latter, and, on December 1, 1931, he issued the assessment order which is now in question, by which he computed the income, profits or gains of the Indian business under Rule 35 at the sum of £ 38,038 or Rs. 5,14,020. The company appealed against this assessment to the Assistant Commissioner of Income-tax, who confirmed the assessment, and they then requested the Commissioner of Income Tax to refer the matter to the High Court under Section 66 (2) of the Act. The Commissioner took the view that the company's return had not been in the prescribed form and that, accordingly they had failed to make a return, with the result that the assessment was made by the Income Tax Officer under sub-Section (4) of Section 23, and the appeal to the Assistant Commissioner was incompetent. Accordingly, as the matter was of importance, he made the reference on his own motion under Section 66 (1). While the point does not directly concern the questions of law referred, their Lordships feel some doubt as to the Commissioner's view that the Company had failed to make a return within the meaning of Section 22 (4).

The two questions of law referred to the Court are as follows :—

"(1) Whether the Income Tax Officer, Companies Circle, Bombay, was justified in law in resorting to Rule 35 of the Income Tax Rules for the purpose of assessing the company to income tax for the year 1931-32 having regard to the *data* furnished by it to that Officer.

(2) Whether the assessment of the company to income tax for the year 1931-32 is a legal assessment and binding upon it in view of the opinion expressed by this Honourable Court in Civil Reference No. 5 of 1928".

The first question involves the appellant company's challenge of the Income Tax Officer's right to have recourse to Rule 35, while the second question concerns the validity of his application of the rule.

The Income Tax Officer is only authorised to have recourse to the method of computation provided by Rule 35 "in the absence of more reliable data". In the opinion of their Lordships, this requires (*a*) a scrutiny of the *data* which in fact had been made available to the Income Tax Officer, irrespective of any question

as to the validity or correctness of the return made under Section 22 (1) and (*b*) a consideration of the reliability of those *data* for the purpose of a proper computation of the income, profits or gains of the company in accordance with Section 13 of the Act.

The appellant company maintains that the Income Tax Officer had more reliable *data* available (1) in the return made by the company and the revenue account and balance sheet of the Indian business which accompanied it, or, if that view was unsound, (2) in the said documents, supplemented by the triennial valuation reports of the whole business for the triennial period ending on September 30, 1928, and the balance sheet and revenue account of the entire business for the year ended September 30, 1930, in both of which the average rate of interest earned by the invested funds of the company appears.

The method of computation under these contentions was as follows:—Under (1), the total premium income of the Indian business from non-participating policy-holders amounting to £ 90 for the year of account, and interest on investments in India and fees received in India to the amount of £ 3,151, making a total income of £3,241, no claim in fact being made for deduction of the small proportion of the expenses referable to that part of the business. Under (2) it was proposed to add a sum to represent what might be called the share of the Indian business in the interest earned by the total investments of the company held in Australia, by taking the proportion of that interest arrived at on the ratio borne by the total amount of the transfers from the Indian branches to the head office from their inception, shown in the revenue account and balance sheet of the Indian business as at September 30, 1930, to the total of the company's investments at the same date in the company's balance sheet and revenue account, the interest being calculated at the average rate above mentioned.

The view taken by the Income Tax Officer, which was concurred in by the Assistant Commissioner, and is maintained in this case, was that in the case of a life insurance company, the only reliable *data* to arrive at its profits was by a valuation report, and he asked for a separate valuation report of the Indian business for a triennial period. The company declined to give this, but offered—though stating that they were under

no obligation to do so—to send him a separate valuation of their Indian business as at September 30, 1930. A single valuation report as at the end of the year of account would obviously not have been sufficient for the ascertainment of profits; it would be necessary to have a valuation as the *terminus a quo*, and this would be afforded either by a valuation as at September 30, 1929, or, in accordance with the practice of the company, a valuation for a triennial period, under which the ascertained profits might be divided equally between the three years. If a valuation report as at September 30, 1930, can be compiled, there can be no obstacle as Counsel for the company admitted, to the compilation of a similar valuation report as at an earlier date a valuation report over a triennial period is clearly the more convenient course.

While BEAUMONT, C. J., expressed himself as inclined to accept the contentions of the appellants as above stated, both the learned Judges decided the case adversely to the appellants on an argument submitted to them for the first time by the Advocate-General that income earned in Australia on monies remitted by the Indian branches and invested in Australia was liable to tax under Section 42 of the Act. In their Lordships' opinion, any claim as to liability to tax under Section 42 is a matter outside the letter of reference and is irrelevant to the questions submitted. It is an altogether different matter that, in making a valuation of the Indian business, it is necessary to consider the reserves held against the liability on the Indian policies, which in fact are held and invested by the head office. Their Lordships are not concerned in the present case with any possible liability of the company to tax under Section 42, and they express no opinion on the matter.

In the opinion of their Lordships, the Income Tax Officer was entitled to take the view that the income, profits or gains of the Indian business could not properly be deduced from the *data* supplied by the company with the return. Only a small proportion of the premiums received could be said to represent income, profits or gains, and that would have to be taken on an average basis, as there will be losses on individual policies. As regards the appellants' second contention, their Lordships are of opinion that the Income Tax Officer rightly took the view that the information submitted by the appellants did not afford more reliable *data* for computation of the income, profits or gains of

the Indian business than the method prescribed by Rule 35, which is based on the total income, profits or gains of the company, the proportion attributable to the Indian business being calculated on the ratio of the Indian premium income to their total premium income. There can be no doubt that the total income, profits or gains of the company would fall to be computed on the basis of their triennial valuation reports, which in their Lordships' opinion, is the most reliable method of computation in the case of a life insurance company. It is the method applied under Rule 25 in the case of companies incorporated in India. The amount of interest earned on investments, though it is an element in the ascertainment of the income, profits or gains, is not by itself a reliable *datum* for such ascertainment.

Their Lordships are, therefore, of opinion that the Income Tax Officer was justified in resorting to Rule 35.

Applying Rule 35, the Income Tax Officer assessed the company as follows :

	£
(1) Premiums of the company as a whole for the year ended September 30, 1930 ...	3,244,476
(2) Premiums of the company in British India for the same period ...	87,942
(3) Net assessable profit of the company as a whole based on the triennial investigations as at September 30, 1928 ...	1,405,027
Proportionately profit of British India ...	38,083
or, at 1s. 25/32d.—Rs.	5,14,020

As regards (1) and (2) if their Lordships assume without deciding that under Section 35 in its application to the present case the "premium income" should include the premiums received in respect of participating policies, it will still remain that as regards (3) the principle of *Styles'* case (*supra*) has been altogether ignored.

The "total income, profits or gains, of the companies" referred to in Rule 35 is the income, profits or gains as they would be ascertained for the purposes of the Act.

In the assessment order the following attempt is made to meet this manifest objection—apparently by showing that the

figure of £1,405,027, being less than the average receipts (excluding premiums) for a year, is not excessive:—

"According to the Bombay High Court decision the surplus profit arising out of contributions from the participating policyholders is not liable to tax. From the valuation report of the company as a whole for the triennium ended September 30, 1928, it will be seen that the income from sources other than participating and non-participating premiums is £ 4,404,140, *i.e.*, average income for one year is £ 1,468,047 (about). The surplus for the year ended September 30, 1930, based on the abovesaid triennial investigations as intimated is £1,405,027 which is less than the average income of £1,468,047. For the purposes of assessment, it is regarded that the expenditure incurred by the company is first set off against the participating and non-participating premium income and the balance of expenditure against income from other sources. Thus the surplus is regarded as wholly out of income from other sources liable to tax."

This argument cannot be accepted: indeed it is quite inconsistent with the reason for rejection of the appellant's two contentions on the first question. The Income Tax Officer has entirely ignored the non-participating premiums received, and, on the other hand, has included the whole amount of consideration received in respect of annuities. Further, he has deducted nothing in respect of the liabilities of the company, or for the expenses relative to the non-participating business. It is impossible to regard this figure as the proper ascertainment of the income, profits or gains of the company.

Their Lordships are, therefore, of opinion that the assessment was not a valid or legal assessment under Rule 35.

Their Lordships, accordingly, are of opinion that the first question in the letter of reference should be answered in the affirmative, and that the second question should be answered in the negative. They will humbly advise His Majesty that the appeal should be allowed, that the judgment of the High Court should be set aside and that the questions should be answered as above stated. The respondent will pay to the appellants their costs of this appeal and in the Court in India.

Appeal allowed.

Solicitors:—Messrs. *E. F. Turner & Sons*, for the appellant; *The Solicitor, India Office*, for the respondent.

[IN THE MADRAS HIGH COURT.]

K. R. M. T. T. THYAGARAJA CHETTIAR

v.

THE COLLECTOR OF MADURA.

Venkataramana Rao, J.

October 23, 1935.

INCOME TAX—PROCEEDINGS BY COLLECTOR FOR RECOVERY OF ARREARS—APPLICATION FOR WRIT OF *Certiorari* TO COLLECTOR—MAINTAINABILITY—JURISDICTION OF HIGH COURT TO ISSUE WRIT—MATTER CONCERNING REVENUE—'ORIGINAL JURISDICTION' —' ACT DONE ACCORDING TO LAW '—INCOME TAX ACT (XI OF 1922), SECTION 46—GOVERNMENT OF INDIA ACT, 1915, SECTION 106 (2)—LETTERS PATENT.

The petitioner had made default in payment of income tax and certificates as required by Section 46 of the Income Tax Act were issued to the Collector for recovering the arrears. The Revenue Divisional Officer issued an order for arrest of the petitioner. The petitioner applied to the High Court for a writ of certiorari *to quash the proceedings against him under Section 46 on the ground that the proceedings violated Clause (7) of Section 46 in that they were not commenced within the expiration of one year from the last day of the year in which the demands were made and also on the ground that they contravened the provisions of Section 48 of the Revenue Recovery Act:*

Held, *that the High Court had no jurisdiction to issue a writ of* certiorari *as the act complained against concerned revenue.* Held further, *that the High Court had no power to issue the writ even if the proceedings were not in accordance with law, provided the Revenue Officer was under the* bona fide *belief that he was acting according to law.*

High Courts have only such powers in the matter of issuing writs of certiorari *as the Supreme Courts had. The Letters Patent have not enlarged their jurisdiction in this respect.*

The Supreme Courts had no jurisdiction to issue a writ of certiorari *concerning any act ordered or done in the collection of revenue according to the usage and practice of the country or regulations of the Governor-General in Council, and income tax is revenue within the meaning of this rule.*

The words ' original jurisdiction ' in Section 106 (2) of the Government of India Act are not confined to Ordinary Original

Civil Jurisdiction, and writs of certiorari *are issued only in the exercise of the original jurisdiction of the High Court.*

GOVINDARAJULU *v.* SECRETARY OF STATE (I. L. R. 50 Bom. 449), *dissented from.*

The exception referred to in Section 106 (2) of the said Act is not confined to the acts which have been done in strict conformity with law, but applies to acts done in the bona fide *belief that they are in accordance with law.*

Cases referred to :—

ALCOCK, ASHDOWN & CO., LTD. *v.* CHIEF REVENUE AUTHORITY, BOMBAY [1923] (I.L.R. 47 Bom. 742; 50 I.A. 227; 75 I. C. 392; 1 I.T.C. 234).

BEST & CO. *v.* COLLECTOR OF MADRAS [1918] (35 M.L.J. 23; 1 I.T.C. 18; 48 I.C. 790).

GOVINDARAJULU *v.* SECRETARY OF STATE [1926] (I. L. R. 50 Bom. 449).

JOHN CALDER *v.* ROBERT CRAIGIE HALKETT [1839] (2 M.I.A. 293).

PENUGONDA VENKATARATNAM *v.* SECRETARY OF STATE [1930] (I.L.R. 53 Mad. 975).

SPOONER *v.* JUDDOW [1850] (4 M.I. A. 353).

Civil Miscellaneous Petition No. 2544 of 1935.

This was a petition praying that in the circumstances stated in the affidavit filed therewith, the High Court will be pleased to issue a writ of *certiorari* to the Collector of Madura acting under the statutory powers given by Section 46 of the Indian Income Tax Act.

K. V. Krishnaswami Ayyar and *T. R. Ramaswami Iyangar*, for the petitioner.

Government Pleader and *N. Srinivasa Ayyangar*, for the respondent.

ORDER.

VENKATARAMANA RAO, J.—This is an application for the issue of a writ of *certiorari* to quash the proceedings of the Collector of Madura taken in regard to the realisation of the arrears of

income tax levied on the petitioner. The case of the petitioner is that he was assessed to income tax for the years 1931-1932, 1932-1933 and 1933-1934 in the sum of Rs. 5,510-2-0, Rs. 7,503-5-0 and Rs. 8,333-6-0 respectively totalling Rs. 21,766-13-0. The notices of demand for the several years were respectively issued on the 31st January, 1933 and 16th November, 1933. After assessment, proceedings under Section 46 of the Income Tax Act were commenced and certificates as required by the said section were issued. In March 1935, the Revenue Divisional Officer issued an order for arrest of the petitioner for the said arrears and the petitioner was arrested on the 26th March, 1935, when he gave 22 post dated cheques commencing from 1—4—1935 to 6—9—1935 and he was thereafter released and then two of these cheques were cashed but he understands that proceedings for arresting him had already been issued and he seeks to quash them on the ground that they violate Section 46 · (7) of the Income Tax Act in that the proceedings were not commenced within the expiration of one year from the last day of the year in which any demand was made under the Act and also in contravention of the provisions of Section 48 of the Revenue Recovery Act which requires as a condition precedent that there should be wilful default.

On behalf of the Government a preliminary objection has been taken that the jurisdiction to issue a writ is barred under Section 106 (2) of the Government of India Act, and even assuming jurisdiction, no writ can lie for quashing a ministerial act, as in this case what is sought to be quashed is the warrant issued. It was further contended that even the preliminary order in and by which the warrant was directed to be issued is also ministerial. The argument based on Section 106, Clause 2 is thus put: income tax is revenue; the proceedings that are sought to be quashed were in respect of acts ordered or done in the collection thereof and the Collector acted under Section 46 of the Income Tax Act, according to the law for the time being in force. The writ of *certiorari* being an original writ, the jurisdiction is thus barred. It is contended in answer by Mr. K.V. Krishnaswamy Ayyar that Section 106 (2) does not apply to this case as the original jurisdiction in that clause relates only to suits or actions instituted on the original side of the Madras High Court, as Section 106 (2) is nothing but a re-enactment of the saving clause in the Supreme Courts Act (39 and 40 Geo. III Ch. 79) and under that Act the Supreme Court has jurisdiction exercisable only within the limits of the Presidency Town and the saving clause related only to that

jurisdiction. He relied on the Privy Council decision in *Alcock Ashdown & Co., Ltd.* v. *Chief Revenue Authority, Bombay*. He further contended that the act sought be quashed is a judicial act. He also contended even if Section 106 (2) may be said to have taken away the power to issue a writ of *certiorari*, if the act which is sought to be quashed is in excess of the jurisdiction of a body which exercised judicial functions the High Court has power to issue a writ of *certiorari* in the exercise of its inherent jurisdiction.

Before examining the soundness of these contentions, it will be necessary to refer to the relevant provisions of the various statutes which define the scope and extent of the power to issue the writ of *certiorari* possessed by the High Court. The jurisdiction which the High Court has to issue writs of *certiorari* or other prerogative writs is derived from the Supreme Court and it has in this respect only such jurisdiction as the Supreme Court had. The Supreme Court of Madras was established by the Government of India Act, 1860 (39 and 40 Geo III, Ch. 79). It provided for the establishment of a Supreme Court of Judicature at Madras......... "with full power to exercise jurisdiction...........and to be invested with such power and authorities, privileges and immunities......and subject to the same limitations, restrictions and control within the said.........Town of Madras and Territories dependent on the Government of Madras......as the said Supreme Court of Judicature at Fort William in Bengal......invested with or subject to within the said Fort William or the Kingdoms or provinces of Bengal, Behar and Orissa."

Therefore it is necessary to note what were the powers and limitations of the Supreme Court at Fort William in 1800. The Supreme Court at Fort William was itself established by virtue of the East India Act, 1772, (13 Geo. III. Ch. 63). Under the Letters Patent by which the Supreme Court of Bengal was constituted, one of the powers it had was the power to issue a writ of *certiorari* conferred on it by Section 4 of the Letters Patent. It is a well known fact that owing to the conflict which arose between the Judges of that Court and the Executive Government it was thought desirable to define and restrict the powers of the Supreme Court. Accordingly 21 Geo. III. Ch. 70 was passed. Among others there were two limitations imposed on the powers of the Supreme Court:

(1) " That the Governor-General in Council of Bengal shall not be subject jointly or severally, to the jurisdiction of the Supreme

Court of Fort William in Bengal for or by reason of any act or order, or any other matter or thing whatsoever counselled, ordered or done by them in their public capacity only, and acting as Governor-General and Council."

(2) " And............the said Supreme Court shall not have or exercise any jurisdiction in any matter concerning the revenue or concerning any act or acts ordered or done in the collection thereof, according to the usage and practice of the country, or the regulations of the Governor-General in Council."

It will thus be seen that in two matters, *i.e.*, in regard to the jurisdiction over the Governor-General and Council and in regard to matters concerning revenue, the jurisdiction had been curtailed.

These limitations again were emphasised and enacted by 39 and 40 Geo. III, Ch. 79 and by the Letters Patent which were issued in pursuance thereof constituting the Supreme Court of Judicature at Madras. The Letters Patent provided in Clause 8 "that the said Chief Justice and the said puisne Judges shall severally and respectively be, and they are, all and every one of them hereby appointed to be, Justices and Conservators of the Peace, and Governors within and throughout the settlement of Fort St. George, and the Town of Madras, and the limits thereof, and the factories subordinate thereto, and all the territories which now or, are hereafter may be, subject to or dependent upon, the Government of Madras aforesaid, and to have such jurisdiction and authority as our Justices of Our Court of King's Bench have, and may lawfully exercise, within that part of Great Britain called England, as far as circumstances will permit". It is in virtue of this clause that the Supreme Court derived the power to issue a writ of *certiorari.* The proviso in the Letters Patent defined the exception to the jurisdiction of the court. The relevant provision ran as follows :—

" Nor shall the said Court have or exercise any jurisdiction in any matter concerning the revenue, under the management of the said Governor and Council respectively either within or beyond the limits of the said Town or the Forts or the Factories subordinate thereto, or concerning any act done according to the usage and practice of the country or the regulations of the Governor in Council."

The Supreme Court had no power to issue a writ of *certiorari* or other prerogative writs in matters concerning revenue within or beyond the limits of the Town of Madras or the Forts or Factories

subordinate thereto. The present High Court was constituted under the Indian High Courts Act, 1861 (24 and 25 Vict. Ch. 104). Section 9 of that Act runs as follows :

"Each of the High Courts to be established under this Act shall have and exercise all such Civil, Criminal, admiralty and vice-admiralty, testamentary, intestate and matrimonial jurisdiction, original and appellate and all such powers and authority for and in relation to the administration of Justice in the Presidency for which it is established, as Her Majesty may by such Letters Patent aforesaid grant and direct subject however, to such direction and limitation as to the exercise of original Civil & Criminal jurisdiction beyond the limits of the Presidency Towns as may be prescribed thereby; and save as by such Letters Patent may be otherwise directed and subject and without prejudice to the Legislative powers in relation to the matters aforesaid of the Governor-General of India in Council the High Court to be established in each Presidency shall have and exercise all jurisdiction and every power and authority whatever in any manner vested in any of the Courts in the same Presidency abolished under this Act at the time of the abolition of such last mentioned Courts."

Dealing with this Section VENKATASUBBA RAO, J., observed in *Penugonda Venkataratnam* v. *Secretary of State* :

"they (the Letters Patent) contain in fact, no provision corresponding to Clause 8 of the Charter of 1800. The High Court, therefore, derives its power to issue prerogative writs not from any express clause in the charter, but from Section 9 of the Act, which preserves intact the powers of the abolished Courts. It follows therefore that the Letters Patent have not enlarged the jurisdiction of the High Court in *certiorari*."

Section 106 of the Government of India Act does not carry the matter further. Section 106 (1) is as follows :—

"106 (1). The several High Courts are Courts of record and have such jurisdiction original and appellate, including admiralty jurisdiction in respect of the offences committed on the high seas and all such powers and authority over or in relation to the administration of justice including power to appoint clerks and other ministerial Officers of the Court, and power to make rules for regulating the practice of the Court, as are vested in them by Letters Patent, and subject to the provisions of any such Letters Patent, all such jurisdictions, powers and authority as are vested in these Courts respectively at the commencement of this Act."

Therefore the question is, had the Supreme Court the power to issue a writ of *certiorari* in regard to matters of revenue and if so, subject to what limitations? As will be seen from the provisions of the statutes already stated, it had no jurisdiction to issue a writ of *certiorari* concerning any act ordered or done in the collection of revenue according to the usage and the practice of the country or the regulations of the Governor and Council. If the Supreme Court had no jurisdiction to issue a writ of *certiorari*, the High Court has no jurisdiction to do so. This application for the issue of a writ is not therefore, maintainable. I am also of opinion that the application is unsustainable in view of Section 106, Clause 2. I shall now deal with the contention of Mr. Krishnaswami Ayyar on this point. In one sense his argument is self-destructive. According to him the jurisdiction of the Supreme Court to issue a writ of *certiorari* was confined only to the Presidency Town because the jurisdiction of the Supreme Court can only be exercised within the limits of the Presidency Town and not beyond it. If so, the High Court's jurisdiction being only such jurisdiction which the Supreme Court had, his application to this Court for the writ of *certiorari* cannot lie. I do not agree with Mr. Krishnaswami Ayyar that the phrase 'original jurisdiction' in Section 106 (2) should be confined to Ordinary Original Civil Jurisdiction. There is no doubt an observation of the late Chief Justice in *Govindarajulu* v. *Secretary of State* which appears to lend support to the contention of Mr. Krishnaswamy Ayyar. The learned Chief Justice on page 445 commenting on Section 136, Clause 2 of the Government of India Act observes thus:

"In matters affecting the revenue, the original side of this Court and that side alone is debarred from interfering in revenue matters."

The learned Subordinate Judges in that case were not considering the power of the High Court to issue a writ of *certiorari*. Under Section 106, it will be seen the High Court is vested with (1) the original jurisdiction more specifically described in Clauses 12 and 13 of the Letters Patent and, (2) the original jurisdiction of the abolished Supreme Court which is conferred by the words 'such jurisdiction, powers and authority as are vested in those Courts respectively at the commencement of this Act.' It is not disputed that the writ of *certiorari* is issued in the exercise of original jurisdiction (I.L.R. 53 Mad. at 999 and 1017). As an exception to both sets of original jurisdiction above mentioned Section 106 Clause 2

has been enacted, just as they have enacted Section 110 in regard to exemption conferred in favour of the Governor and Council. The wording of Section 106 (2) is in my opinion very suggestive and instructive. The words 'have not' and 'may not' are both declaratory and prospective and would aptly comprise also the jurisdiction vested in the Court at the commencement of the Act apart from the jurisdiction vested by the Letters Patent.

Considerable stress was laid by Mr. K.V. Krishnaswami Ayyar on the decision of the Privy Council in *Alcock Ashdown & Co., Ltd.* v. *Chief Revenue Authority, Bombay.* In that case the Income Tax Officer refused to refer a case to the High Court of Bombay under Section 51 of the Income Tax Act of 1918. Both the Bombay High Court and the Madras High Court had taken the view that an order under Section 45 of the Specific Relief Act could not be issued compelling the Income Tax Officer to refer the case to them because of Section 106 (2) of the Government of India Act. Their Lordships of the Judicial Committee negatived this view and held that 'the order of a High Court to a revenue officer to do his statutory duty would not be the exercise of original jurisdiction in any matter concerning the revenue." As I understand their observation, in their Lordships' view to ask a revenue officer to do his statutory duty would not be a matter concerning revenue. This is made clear by a passage from the previous paragraph :—

"To argue that if the legislature says that a public officer even a revenue officer shall do a thing, and he without cause or justification refuses to do that thing, yet the Specific Relief Act would not be applicable and there would be no power in the Court to compel him to give relief to the subject is to state a proposition to which their Lordships must refuse to assent."

Two things are necessary to constitute a bar under Section 106 (2), *viz.*, (1) an exercise of original jurisdiction (2) a matter concerning revenue or the collection thereof. In their Lordships' view as aforesaid there was no matter concerning revenue in this case. I do not think their Lordships meant to decide there was no exercise of original jurisdiction as Section 45 of the Specific Relief Act refers to ordinary original civil jurisdiction.

Mr. Krishnaswamy Ayyar attempted to argue that the income tax is not revenue but this argument is not open to him after the ruling in *Best & Co.* v. *Collector of Madras.*

Another argument of Mr. Krishnaswamy Ayyar may be noticed, namely, even if the statute has taken away the writ, when a judicial body acts *ultra vires* this Court can nevertheless issue a writ. The short answer to this is that the High Court had never any jurisdiction to issue the writ in matters concerning revenue.

It was next contended by Mr. K. V. Krishnaswamy Ayyar that the exception can only be in favour of acts which have been done according to the law for the time being in force and therefore if the act is not in conformity with the law and in direct contravention of it the jurisdiction is not barred. In this case the Collector having acted in contravention of Section 46, Clause 7, he must be deemed to have not acted according to the law for the time being in force I am unable to accept this contention. This claue was interpreted very clearly by their Lordships of the Judicial Committee in *Spooner* v. *Juddow*. In that case it was found that the Collector illegally levied quit rent from a person who was not liable to pay it. Dealing with the argument that the exception of jurisdiction would avail only when the act is according to the regulations of the Governor and Council, LORD CAMPBELL observed:

"There can be no rule more firmly established than that if parties *bona fide* and not absurdly believe that they are acting in pursuance of statutes and according to law they are entitled to the special protection which the legislature intended for them although they have done an illegal act."

His Lordship concluded the judgment thus:

"We are bound to differ from the judge below who says 'that the jurisdiction of this Court has not been taken away when the act complained of is not warranted by the usage and practice of the country or by the company's regulation'. If it concerned the revenue or was a matter concerning an act *bona fide* believed to be done according to the Regulations of the Governor and Council of Bombay his jurisdiction was gone although *prima facie* it appeared to be a trespass over which his jurisdiction might be properly exercised."

Mr. K. V. Krishnaswamy Ayyar sought to distinguish this case by relying on the observations of Baron Parke in *John Calder* v. *Robert Craigie Halkett*. In that case there was an action on trespass brought to recover damages for the arrest and false imprisonment of the plaintiff by the Magistrate of

Foujdari (criminal) of the Zillah of Nuddeah in Bengal. The action was held not to lie by virtue of 21 Geo. III, Ch. 70, Section 24. It prohibited an action against any person exercising a judicial office for an act done by virtue of the order of the Court. Dealing with this his Lordship observed :

"The object is to put the judges of the Native Courts on the footing of the Judges of the Supreme Courts of Record or Courts having similar jurisdiction to the Native Courts here, protecting them from actions for things done within their jurisdiction though erroneously or irregularly done, but leaving them liable for things done wholly without jurisdiction."

The question in this case is entirely different. It is not merely exemption from liability in a personal action. In 4 M.I.A. 353, their Lordships considered the jurisdiction of the Court from the point of view of the subject matter and ruled that in respect of the subject matter the jurisdiction of the Court had been entirely taken away if the officer acted in the belief that he had jurisdiction. In the present case it is not denied that certificates were issued in accordance with the provisions of Section 46 of the Income Tax Act, and orders for arrest made and warrants issued in pursuance of the said provision. Whether the said orders were justified on a right construction of the said provision does not matter ; but what matters is whether the Collector *bona fide* believed that he was acting according to the said provision. If so, the jurisdiction of the Court to deal with the said act is gone. In this case it has been conceded that the Collector was not acting *mala fide*. I have therefore come to the conclusion that the preliminary objection must prevail and that this court has no jurisdiction to issue a writ of *certiorari* to quash the proceedings concerned. I therefore dismiss the petition with costs, *viz*., Rs. 100 (to be paid by the petitioner).

[IN THE NAGPUR JUDICIAL COMMISSIONER'S COURT.]

SIR BISESARDAS DAGA AND OTHERS, *In re.*

Subhedar and Niyogi, Addl. J. Cs.

January 7, 1935.

INCOME TAX—HINDU UNDIVIDED FAMILY—SEPARATION OF MEMBERS—REGISTRATION AS FIRM—REFUSAL IN SUBSEQUENT YEAR TO RENEW CERTIFICATE OF REGISTRATION ON THE GROUND THERE WAS NO SEPARATION—LEGALITY—INCOME TAX ACT (XI OF 1922), SECTION 25-A—INCOME TAX RULES, RULE 6.

Where an Income Tax Officer finds after an inquiry under Section 25-A of the Income Tax Act, that a separation of the members of a Hindu family, which had till then been assessed as an undivided family, has taken place and registers the members of the family as a firm, it is not open to him, in view of the provisions of sub-Clause (3) of Section 25-A and Rule 6 of the Income Tax Rules to refuse to renew the registration of the members as a firm in a subsequent year on the ground that the previous finding that the members had separated was wrong and that the members had not in fact separated.

Cases referred to:

BIRADHMAL LODHA *v.* COMMISSIONER OF INCOME TAX [1934] (2 I. T. R. 164; I. L. R. 56 All. 504).

MATHRADAS *v.* COMMISSIONER OF INCOME TAX, PUNJAB [1933] (1 I. T. R. 212; A. I. R. 1933 Lah. 815).

SHER SINGH *v.* COMMISSIONER OF INCOME TAX, PUNJAB [1934] (2 I. T. R. 479; A. I. R. 1935 Lah. 81).

Case stated by the Commissioner of Income Tax, Central and United Provinces under Section 66 (2) of the Indian Income Tax Act (XI of 1922), [Mis. Judicial Case No. 56 of 1936].

The necessary facts are stated in the judgment:—

Sir Hari Singh Gour, for the assessees.

Rai Bahadur D. N. Chaudhury, for the Commissioner.

ORDER.—This case arises on a statement submitted to this Court by the Commissioner of Income Tax under Section 66 (2), Indian Income Tax Act, XI of 1922.

2. Prior to 1929-30 the assessee was admittedly an undivided Hindu family consisting of Sir Bisesardas Daga who was the

manager and his younger brothers, Seth Narsinghdas Daga, Seth Badridas Daga and Seth Ramnath Daga, a minor. In the course of the assessment proceedings of 1929-30 it was alleged that the joint Hindu family had constituted itself into a firm, as a result of a declaration of unequivocal intention to separate made in writing on the 10th February 1928 on a duly stamped paper followed by a registered deed of partnership dated 30-7-1928. Out of the property which consisted of villages, houses, money-lending and other business and jewellery, there had been already actual division of some immoveable property and jewellery at Bikaner. The property in British India remained undivided as before but the disruption of the joint family was evidenced by splitting up the capital accounts of their business into four accounts with equal amounts in the names of four brothers. No alteration in the register of proprietary mutations was made in respect of the villages. It was alleged that the declaration as to partition had come into force from the 1st April, 1928.

3. All the four brothers jointly applied for registration of their firm under Section 2 (14) and the then Income Tax Officer, Mr. Subhedar, passed a formal order on 20-3-1930 to the effect "that the joint family had ceased to exist even though there had been no division by metes and bounds of the villages and houses, (Appendix A), and accordingly registered the instrument of partnership dated 30-7-28 on 22nd March, 1930, (Appendix B). This registration was renewed for 1930-31 and 1931-32 by Mr. Bagri who had succeeded Mr. Subhedar in those years as Income Tax Officer. The application for renewal of registration for 1932-33 was, however refused, and the Income Tax Commissioner declined to state the case under Section 66 (2) of the Income Tax Act. The assessee did not move further in the matter as he was not assessed to any income-tax in that year.

4. The question again arose in respect of the assessment year 1933-34 and the Income Tax Officer by an order passed on 28-2-1934 declined registration as a result of fresh enquiries disclosing that that the assessee continued to be a Hindu joint family in spite of the declaration dated 10-2-28. An appeal made to the Assistant Commissioner of Income Tax having failed, the assessee applied to the Commissioner of Income Tax for reviewing the adverse orders passed against him and also to draw up a statement of the case and refer for the decision of this Court. The Commissioner of Income Tax has therefore referred the question in these terms:—

"In all the circumstances of this case, having regard to the facts that there was no finding at any time to the effect that the Hindu undivided family represented by the assessee had disrupted and that joint family property had beed divided among the various members in definite portions, was the Income Tax Officer justified in holding that the so-called firm, of which registration under Section 26-A was sought for and refused, was only a subterfuge for the purposes of obtaining a reduction in the liability to income tax and super tax?"

This reference raised two questions; (1) whether there was no finding at any time to the effect that the undivided family had been divided, and (2) whether the Income Tax Officer was justified in holding that the firm which had been registered for 2 years under Section 26-A and assessed as such was not a firm.

5. It is pertinent to notice that in regard to the assessment year 1933-34 the assessee had only applied for renewal of the registration of his firm under Section 26-A in the form 1 given at page 70 of the Income Tax Manual. According to Rule 6 of the Rules framed by the Board of Inland Revenue, in exercise of the powers conferred by Section 59 of the Indian Income Tax Act, 1922, the Income Tax Officer is bound to renew the certificate from year to year on an application made to him in that behalf accompanied by a certificate signed by one of the partners of the firm that the constitution of the firm as specified in the instrument of partnership remained unaltered. It is clear that the Income Tax Officer would have no power to decline to renew the certificate of registration unless the firm had altered its constitution since the grant of the previous certificate. In neither of the two orders dated 23-11-32 and 28-2-34 passed by the Income Tax Officer is there anything to show that since the date when the certificate was last renewed, namely 15-3-1932, there was any change in the constitution of the firm.

6. The Income Tax Officer was influenced by certain registered deeds and certain averments made in a plaint prior to 1930 in reaching the conclusion that the assessee had not ceased to be a joint family notwithstanding the declaration and the instrument of partnership of 1928. In doing so the Income Tax Officer exercised a power which is not contemplated by Rule 6 of the aforesaid rules. It was perhaps to circumvent this difficulty that the Commissioner of Income Tax took the stand that there had been no finding at any time to the effect that the Hindu undivided family

had disrupted and that the joint family property had been divided in definite portions. This position was undoubtedly forced on the Commissioner by reason of the terms of sub-Section 3 of Section 25-A of the Income Tax Act, which says when such an order has not been passed in respect of a Hindu family hitherto assessed as undivided such family shall be deemed for the purposes of the Act to continue to be a Hindu undivided family. It is urged that there was no specific order passed under Section 25-A as there was no enquiry preceded by notices to all the persons concerned. This is contradicted by the express wording of Mr. Subhedar's order passed on 20th March, 1930. There he states that all the four brothers applied for registration of their firm on the ground that they had ceased to be a joint family and that "as the result of enquiry" he found that they had really separated in mess, worship, purse and residence. He was satisfied from the declaration dated 10-2-28 and the deed of partnership dated 30-7-28 and also by the distribution of capital in each branch that the joint family had ceased to exist although the villages and houses were not divided by metes and bounds. He no doubt remarked that in future years the matter would have to be reconsidered in view of the subsequent conduct of the parties. When the Officer who passed the order states in unequivocal terms that he made an enquiry we are unable to accept the allegation that there was no such enquiry. Nor do we think that there was any necessity for issuing notices to the members of the family when all of them had joined in making the application. In any case none of them has come forward to repudiate the declaration and the instrument of partnership. In face of these facts it is impossible to contend that Mr. Subhedar's order was not one passed under Section 25-A which had come into force from 1-4-1928. As there was an order under Section 25-A in clear and unequivocal terms sub-Section 3 of Section 25-A must operate to preclude any fresh enquiry.

7. It is urged by the learned counsel for the Commissioner of Income Tax that the firm of which registration was sought was found by the Income Tax Officer to be only a camouflage for obtaining a reduction in the liability to income tax and super tax and that this finding being one of fact cannot be challenged here. The contention would be perfectly sound if the Income Tax Officer was competent to go into the question and give his finding but it has already been shown that he was precluded from doing so by Rule 6 of the Rules framed by the Board of Inland Revenue as well as by sub-Section 3 of Section 25-A. It may be conceded that the

Income Tax Officer is ordinarily not bound by the correctness of any previous orders passed by him but that power is, so far as this case is concerned, expressly withdrawn by sub-Section 3 of Section 25-A, and Rule 6 of the aforesaid rules makes it imperative on him to renew the certificate except when it is proved that the constitution of the firm has altered since the grant of the last certificate. The case in *Mathra Das.* v. *Commissioner of Income Tax* relied on by the learned Commissioner is distinguishable on facts inasmuch as it was found that the partition could not be effected by the execution of a will which could not obviously come into force until the testator's death.

8. We are in respectful agreement with the view taken in *Biradhmal Lodha* v. *Commissioner of Income Tax* and *Sher Singh* v. *Commissioner of Income Tax* that Section 25-A does not demand a partition by metes and bounds. This view is even accepted by the Commissioner of Income Tax himself. At any rate in respect of the extensive business which the assessee carries on at diverse places in and outside British India the partition by metes and bounds is an impossibility. The real question is whether the four brothers have gone back upon their declaration of 1928 and have reverted to their former position as members of a joint family. There is no evidence of any acts or declarations subsequent to Mr. Subhedar's order to sustain the conclusion that the firm was a subterfuge. Apart however from the merits of the case we are definitely of opinion that in view of the order passed by Mr. Subhedar, the Income Tax Officer was precluded by sub-Section 3 of Section 25-A and Rule 6 from making a fresh enquiry under Section 25-A (1) which itself had no application to this case as the assessee could not, at the time when the Income Tax Officer was making an assessment under Section 23 for the year 1933-34, be described as a Hindu family " hitherto assessed" as undivided. If as the Commissioner of Income Tax rightly conceded, there could be disruption of the family without actual partition of the property by metes and bounds, then Mr. Subhedar's order was correct. In consequence of the division of title, there was nothing to prevent the members of the quondam coparcenary from entering into a contract registered as a firm in 1930 and two subsequent years; if so, the Income Tax Officer had no power to refuse renewal of the certificate unless the firm altered its constitution.

9. For the foregoing reasons we answer the question referred to us in the negative. The costs of this reference shall be paid by

the Commissioner of Income Tax to the assessee. Pleader's fee Rs. 200.

[IN THE PATNA HIGH COURT.]

DHAKESHWAR PRASAD NARAIN SINGH

v.

COMMISSIONER OF INCOME TAX, BIHAR AND ORISSA.

Sir Courtney Terrell, C. J., Macpherson and Agarwala, JJ.

March 29, 1935.

INCOME TAX—MONEY-LENDING BUSINESS—ASSESSMENT OF ACCRUED BUT UNREALISED INTEREST—LEGALITY—ASSESSMENT IN PREVIOUS YEARS, EFFECT OF—METHOD OF ACCOUNTING—CASH SYSTEM—MERCANTILE SYSTEM—MIXED CASH AND MERCANTILE SYSTEM—INDIAN INCOME TAX ACT (XI OF 1922), SECTION 13.

The assessee carried on a money-lending business. His books of account consisted of personal accounts of his debtors in which the interest which accrued from year to year was calculated and entered and the amounts actually realised as interest were also entered. But neither the accrued interest nor the realised interest were totalled in an interest account and no profit and loss was computed. There was also a cash book in which the actual realisations were shown but there was no interest ledger. For the purposes of his return for income tax in previous years he totalled the amount of interest which had accrued in the particular year in question. For the year 1931-32 he submitted a statement showing the interest which he had actually received and contended that he could not be assessed upon accrued but unrealised interest but only upon interest realised by him. The question 'whether in the circumstances of the case the assessee was liable to be taxed on his income from money-lending on the mixed cash and accrued basis which had been followed in his assessment of previous years' was referred to the High Court:

Held, Per COURTNEY TERRELL, C. J.—(*i*) *The assessee had not regularly employed any method of accounting within the meaning of Section 13, and his request did not involve any change in the method of accounting but only a change of the method of assessment which should be employed*; (*ii*) *that though it is open to an Income Tax Officer to assess either upon a cash basis or upon a mercantile basis, accrued interest can only be taken into account if a profit and loss account is drawn up and the accrued but unpaid interest*

is brought in as a valued asset; it was not open to the Income Tax Officer to take the accrued interest into the assessment on any other basis and the method of assessment which had been followed by the income tax authorities was in any case erroneous.

AGARWALA, J.—*The assessee had regularly employed a method of accounting even though it was not scientific and as he had taken into account accrued interest in his method of accounting the income tax authorities were entitled to take into account such interest even though it had not been realised. The reference was concluded by the finding of fact that the sum assessed had been ascertained by a method of assessment regularly employed by the assessee.*

MACPHERSON, J.—*Though the mere fact that the assessee had permitted himself to be assessed on sums, to wit, unrealised interest, which are really debts due to him and not profits of his business does not involve a continuance of the method of accounting under which that was done, with the consequent continuance of unwarranted taxation, that was not the position here. What was to be ascertained was the profits as a whole and as the assessee had indicated that in his view the accrued interest was a good asset at its face value and the computation of improvement in the assets had been made in previous years on his own method of accounting in which he took his unrealised interest as profit of the business the assessment made was not erroneous.*

Obiter.—*As the reference stated implied that the assessee had treated the accrued interest as received by him and as profits of his business during the year, the real contention of the assessee was not raised in the reference in the form in which it was made. A reference may be possible on future material in which the question really raised by the assessee might properly arise for decision.*

Cases referred to:

ANGLO-PERSIAN OIL CO. *v.* COMMISSIONER OF INCOME TAX, BENGAL [1933] (I.L.R. 60 Cal. 843; 1 I.T.R. 129; 37 C. W. N. 430).

COMMISSIONER OF INCOME TAX, BENGAL *v.* SHAW WALLACE & Co. [1932] (6 I.T.C. 178; A.I.R. 1932 P.C. 138).

COMMISSIONER OF INCOME TAX, BIHAR AND ORISSA *v.* MAHARAJA OF DHARBHANGA [1934] (12 Pat. 318; 1 I.T.R. 94; 6 I. T. C. 402.

BOARD OF REVENUE *v.* PYDAH VENKATACHALAPATHY GARU [1922] (1 I.T.C. 185; 69 I.C. 405; A.I.R. 1922 Mad. 426).

FOSTER *v.* COMMISSIONER OF INCOME TAX, BURMA [1929] (3 I.T.C. 435).

NARAIN DAS BHAGWAN DAS *v.* COMMISSIONER OF INCOME TAX, PUNJAB [1933] (7 I.T.C. 135).

PURAN MAL *v.* COMMISSIONER OF INCOME TAX, PUNJAB [1926] (2 I.T.C. 236).

SECRETARY TO THE BOARD OF REVENUE, MADRAS *v.* AR. AR. RM. ARUNACHALAM CHETTIAR [1922] (1 I.T.C. 75).

SHIVA PRASAD GUPTA *v.* COMMISSIONER OF INCOME TAX, C.P. AND U.P. [1929] (124 I.C. 467; 3 I.T.C. 406).

SPANISH PROSPECTING CO., *In re.* [1911] (L. R. 1911 1 Ch. 92).

ST. LUCIA USINES AND ESTATES CO., LTD. *v.* COLONIAL TREASURER OF ST. LUCIA [1924] (L.R. 1924 A.C. 508).

Case stated by the Commissioner of Income Tax, Bihar and Orissa, under Section 66 (2) of the Indian Income Tax Act (XI of 1922). Mis Jud. Case No. 122 of 1933.

The facts are fully stated in the judgment.

Sir Sultan Ahmad, P. R. Das, K. P. Jayaswal and *S. N. Ray*, for the assessee.

Manohar Lal, for the Commissioner.

JUDGMENT.

COURTNEY TERRELL, C. J.—The assessee has amongst other sources of income a money lending business. He keeps books of account which show the business transacted with each debtor, the interest which has accrued and the amount actually realized in each year. In paragraph 4 of the order of the Assistant Commissioner of Income Tax the following facts are set forth: The money lending accounts of the assessee consist of personal accounts of his debtors in which the accrued interests from year to year are calculated and entered. The amount actually realised is also similarly entered, but neither the accrued interest nor the realised interest are totalled and accounted for in an interest account and no profit or loss is computed. There is also a cash book in which the actual realisations are shown, but there is no interest ledger. Clearly therefore the assessee has not computed his profit at all and no

particular method of accounting can be said to be regularly employed by him. The Income Tax Officer had therefore to make the computation of profit upon such basis and in such manner as the Income Tax Officer might determine, and he decided to adopt the accrued basis which was also followed in previous years without objection on the part of the assessee". It appears that the assessee for the purposes of his return for income tax in previous years totalled the amount of interest which had accrued in the particular year in question and paid tax on the amount so found. He now contends that he should not have been assessed in the past on the sums entered in this books as accrued interest and for the current year he desires to correct this situation by demanding to be assessed not upon the interest which has accrued during the year but upon the sums actually received by him.

Now, there are two methods of accounting for the income, profits and gains of a business which are generally referred to as the cash basis and the mercantile basis. According to the former a record is, as in this case, kept of actual receipts and actual payments, entries being made only when money is actually collected or disbursed and if the profits of the business are accounted for in this way the tax is payable on the difference between the receipts and the disbursements for the period in question. There is, secondly, the mercantile system under which a profit and loss account is maintained. At the end of the financial year the assets and liabilities are valued and entered in the account and the difference between the two is the profit upon which the tax is paid. In most cases the debts would be valued as of their face value, that is to say, at the moment at which it is shown as having accrued. Nevertheless the accounting is on a valuation basis and the debts in so far as they are entered in the accounts are considered in the light only of an asset. In this case the finding of fact by the Assistant Commissioner is that the assessee did not compute his profit by either of these two methods or at all. He merely brought his accounts and submitted to be assessed upon the debts which had accrued. If he had adopted the mercantile method and had valued the debts which had accrued to him at the end of the year and had balanced upon the assets against the liabilities he would have been rightly liable to tax upon the profits shown in accordance with that method of accounting. The assessee has however done nothing of the kind. It is true that he has kept accounts and that he has shown debts realised and debts which had accrued but he has nowhere accounted for the profits of the money-

lending business. The Commissioner of Income Tax notwithstanding this finding on the part of the Assistant Commissioner which is set forth in his statement of the case has held that whereas the assessee has hitherto been taxed upon the debts which have accrued to him he cannot now be allowed to say that this system of taxation is erroneous. He attributes to the assessee a desire to change his method of accounting and sets forth a motive on the part of the assessee for desiring to change the method of assessment. This motive, even if the Commissioner's opinion be well-founded, is in my opinion, entirely irrelevant. The accounts which have been supplied for the current year are precisely like the accounts which have hitherto been kept by the assessee and were furnished by him as a basis for assessment. The assessee has made and desires to make no change in his method of keeping accounts. Neither in this year nor in past years has he computed the profit or loss on his business and therefore according to the proviso to Section 13 of the Income Tax Act it is open to the Income Tax Officer to make the computation of income, profits or gains upon such basis and in such manner as the Income Tax Officer may determine. This however does not mean that the Income Tax Officer is at liberty to tax what is not chargeable to income-tax under the Act and if it be true that in past years the Income Tax Officer with the assent of the assessee has taxed that which under the Act is not assessable this is no justification for continuing such a practice. An assessee may well discover that in past years he has paid his tax on an erroneous basis or has returned as profit that which was not profit at all. This fact will not prevent him in any given year from making a return on a correct basis. In this case the Commissioner considers that the assessee wishes to change his method of accounting from the cash basis to the accrued basis. In my opinion this is not a correct view of the matter. The method of accounting now presented is precisely similar to that heretofore followed. What the assessee desires to change is not the method of accounting for profits and gains but the method of assessment which the Income Tax Officer should employ. The question therefore really is whether the assessee is right in his contention that in future the actual sums realised in any year should be taxed, or whether the method heretofore followed in his case of taxing the accruals is correct.

In my opinion amounts which have accrued but which have not been paid do not furnish a basis for taxation unless they appear in a properly balanced profit and loss account as assets in the shape

of outstanding debts and this method cannot be employed unless a regular profit and loss account of the business for the year is supplied. The finding of fact is that this has not been done although possibly it might have been done. It is not obligatory upon the assessee to present his account of profit and loss in this manner. He may elect, as he has done in this case, to be taxed upon the actual receipts less the actual expenses. In my opinion the first paragraph of Section 13 of the Income Tax Act has little or no application to the facts of the case. This section applies only to cases in which the assessee has not merely kept true and accurate accounts of his dealings but has also according to a proper system of book-keeping set forth according to some consistent method his statement of income, profits and gains.

The cases decided before 1922 when the present Income Tax Act came into force have little application. It is now possible for an assessee of a business to keep his account of profits and gains in any form he chooses provided that the profits and gains are thereby properly displayed according to a consistent system.

Therefore debts which have accrued but have not been paid may be set forth in the accounts and the principles which were relied upon by the Full Bench of the High Court of Madras in *Secretary to the Board of Revenue, Income Tax, Madras* v. *Arunachalam Chettiar* are no longer applicable but such debts must be shown as an asset and having been valued they must be shown in a profit and loss account. The finding of the Income Tax Commissioner is that the assessee has never properly accounted for the profits and gains of his business. Accordingly the profits and gains cannot be computed " in accordance with the method of accounting regularly employed by the assessee." There is furthermore no question of the assessee changing his method of accounting; for the accounts now supplied are precisely similar to those supplied heretofore. The matter of assessment must be approached therefore as though the year of assessment in question were the first in which the business had been carried on and the merits of the basis of assessment must be considered *de novo*. The nature of the word "profits" was discussed by the Court of Appeal in England in *In re: The Spanish Prospecting Company, Limited* and LORD JUSTICE MOULTON at page 98 said:

" The word " profits " has in my opinion a well-defined legal meaning, and this meaning coincides with the fundamental conception of profits in general parlance, although in mercantile

phraseology the word may at times bear meanings indicated by the special context which deviate in some respects from this fundamental signification. "Profits" implies a comparison between the state of a business at two specific dates usually separated by an interval of a year. This can only be ascertained by a comparison of the assets of the business at the two dates.

For practical purposes these assets in calculating profits must be valued and not merely enumerated. An enumeration might be of little value. Even if the assets were identical at the two periods it would by no means follow that there had been neither gain nor loss, because the market value—the value in exchange—of these assets might have altered greatly in the meanwhile. A stock of fashionable goods is worth much more than the same stock when the fashion has changed. And to a less degree but no less certainly the same considerations must apply to buildings, plant and other fixed assets used in the business, because one form of business risk against which business gains must protect the trader is the varying value of the fixed assets used in the business. A depreciation in value, whether from physical or commercial causes, which affects their realizable value is in truth a business loss.

We start therefore with this fundamental definition of profits, namely, if the total assets of the business at the two dates be compared, the increase which they show at the later date as compared with the earlier date (due allowance, of course, being made for any capital introduced into or taken out of the business in the meanwhile) represents in strictness the profits of the business during the period in question......To render the ascertainment of the profits of a business of practical use it is evident that the assets, of whatever nature they may be, must be represented by their money value. But as a rule these assets exist in the shape of things or rights and not in the shape of money. The debts owed to the company may be good, bad or doubtful. The figure inserted to represent stock in trade must be arrived at by a valuation of the actual articles. Property of whatever nature it be, acquired in the course of the business has a value varying with the condition of the market. It will be seen, therefore, that in almost every item of the account a question of valuation must come in".

The question formulated by the Income Tax Commissioner is as follows:—"Whether in the circumstances of this case the assessee is liable to be taxed on his income from money lending on the mixed cash and accrued basis, which has been followed in his

assessments of previous years". The statement of the question is followed by the following observation: "As a matter of fact the assessee has been assessed neither on a strictly cash basis nor on accrual basis" and then follows a statement of the way in which the assessee submitted his accounts as found by the Assistant Commissioner. The facts are perfectly clear and are clearly found by the Assistant Commissioner and it is clear that there has been no proper accounting for profits. The answer to the question in my opinion is that the method of assessment heretofore followed was in any case erroneous. It is open to the Income Tax Officer to assess the assessee either upon a cash basis or upon a mercantile basis but in the latter case the accrued interest can only be dealt with if a profit and loss account is drawn up and the accrued but unpaid interest is brought in as a valued asset and it is not open to the Income Tax Officer to take accrued interest into the assessment on any other basis.

AGARWALA, J.—The assessee, who is a large landowner also carries on the business of a money-lender. For the year 1931-32 he was assessed at Rs. 50,987 in respect of the profits of this business. The figure was arrived at by adding together (*i*) the interest on loans which accrued during the year but was not received and (*ii*) the interest received, less the amount taxed in previous years. The assessee objects to the assessment and claims that in respect of the money-lending business he is assessable only on the sum of Rs. 222, which is the amount actually realised in the year in question less deductions on account of sums assessed in previous years. The Commissioner of Income Tax, in stating the case, has said that the sum assessed has been arrived at in accordance with the method of accounting regularly employed by the assessee for a number of years previous to 1931-32.

It appears from the statement of the case that for a number of years the assessee, in his return of income to the Income-Tax Officer, has filled in a certain sum as being his profits from business (the sum varying each year) and with his return has filed two statements showing, respectively: (*a*) the interest accrued during the year but not received and (*b*) the interest received less the portions of it assessed in previous years. The amount entered in the return of income tax has in each year been the total of (*a*) and (*b*).

Section 10 (i) of the Income Tax Act provides: "The tax shall be payable by an assessee under the head " business in respect of the profits or gains of any business carried on by him." Section 13

the business is closed down, for a trader may, for a long period of time, receive in the aggregate large sums of money, but if an unforeseen calamity results in the destruction of his premises and stock the loss may be greater than all his previous receipts. In a commercial sense, however, it is possible to ascertain from time to time whether the turnover of a business is resulting in a profit or not. It is in this sense that the phrase "profits and gains" is used in the Act and in this sense a money-lending business does not differ from any other class of business. What has to be ascertained for the purposes of the Act is neither the receipts of the proprietor of the business nor the profits on each isolated transaction, but the profits and gains of the business as a whole. As was observed by LORD MACMILLAN in the case of *Commissioner of Income Tax, Bihar and Orissa* v. *Maharajadhiraj of Darbhanya* "what the officer is directed to compute is not the assessee's receipts but the assessee's income and in *dubio* what the assessee himself chooses to treat as income may well be taken to be income and to arise when he so chooses to treat it." In the case of a business substitute the word "profit" for the word "income" and this extract concludes the present reference.

Much reliance was placed by the assessee on the decision of the Privy Council in the case of *St. Lucia Usines and Estates Company, Limited* v. *Colonial Treasurer of St. Lucia* for the contention that "profits and gains", like "income" must be received, or treated as received, before the liability to tax arises. That decision, however, in my view, clearly negatives the contention. In that case a company which had ceased to carry on business in the island of St. Lucia sold its properties. The vendee of one of the properties who had not paid the purchase price, agreed to pay interest, on the amount due, on a certain date. The company was assessed in respect of this interest although it was not paid on the due date, or at all, during the year for which the assessment was made. The Privy Council held that the amount was not assessable in that year. It will be observed that the assessment was in respect of what was considered by the assessing authority to be income, and not in respect of the profits and gains of the company's business, for the company had ceased to carry on business before the year in question. The distinction was clearly indicated by LORD WRENBURY, who delivered the judgment of the Judicial Committee where his Lordship said: "It is said, and truly, that a commercial company in preparing its balance sheet and profit and loss account

is as follows : " Income, profits and gains shall be computed, for the purposes of Sections 10, 11 and 12, in accordance with the method of accounting regularly employed by the assessee". There is a proviso to the section which enables the Income Tax Officer to calculate the profits in cases where no method of accounting has been regularly employed or where, from the method employed, the profits cannot properly be deduced.

Prima facie the reference is concluded by the finding of fact that the sum assessed has been ascertained by the method of accounting regularly employed by the assessees. The assessment, however, is challenged on two grounds. In the first place it is argued that no method of accounting has been regularly employed by the assessee. It is contended that the two statements filed each year with the return did not amount to a method of accounting inasmuch as they did not purport to shew what profit had been made by the assessee. As I understood this argument it went to this length, that as there was no addition of the items in the two statements, no profit or loss account and no balance sheet, there was no method of accounting at all. I am unable to agree. It may be said that the assessee's method of keeping the accounts of his money-lending business is not scientific but it is the method adopted by himself and it is the method by which he has regularly ascertained the sum of which he considered himself to be assessable in respect of the profits of his business.

The next ground on which the assessee challenges the assessment is this; he contends that interest not actually received is not assessable and that if he has previously included in his profits sums which are not taxable that circumstance does not prevent him from raising the point now. It may be conceded at once that an assessee is not liable to be assessed in respect of an amount which is not subject to income tax even though he has permitted himself to be taxed in respect of similar sums in previous years. But is this the case in the present instance? It is contended that interest unrealised in fact, and not treated by the assessee as realised, is not " income." That much may be conceded but what the assessee is to be assessed on under Section 10 of the Act is not the " income " from his business but the " profits or gains " of the business. The receipts from the business, obviously do not constitute the profits and gains of the business, for against the receipts have to be set off the expenditure, or at least so much of the expenditure as is permitted. The actual profits of a business are not ascertainable until

the business is closed down, for a trader may, for a long period o time, receive in the aggregate large sums of money, but if an un foreseen calamity results in the destruction of his premises an stock the loss may be greater than all his previous receipts. In commercial sense, however, it is possible to ascertain from time t time whether the turnover of a business is resulting in a profit o not. It is in this sense that the phrase "profits and gains" is use in the Act and in this sense a money-lending business does nc differ from any other class of business. What has to be ascertaine for the purposes of the Act is neither the receipts of the proprietc of the business nor the profits on each isolated transaction, but th profits and gains of the business as a whole. As was observed b LORD MACMILLAN in the case of *Commissioner of Income Ta Bihar and Orissa* v. *Maharajadhiraj of Darbhanya* "what th officer is directed to compute is not the assessee's receipts but tl assessee's income and in *dubio* what the assessee himself choos to treat as income may well be taken to be income and to ari when he so chooses to treat it." In the case of a business substitu the word "profit" for the word "income" and this extract co cludes the present reference.

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mere cash account but values its book debts and its stock in trade and so on and calculates its profits accordingly. From the practice of commerce and of accountants and from the necessity of the case this is so. But this is far from establishing that income arises or accrues from an investment which fails to pay the interest due". This extract from the judgment clearly shows the recognised distinction besween the basis for calculating income and the basis for calculating profits. It is argued, however, that the assessee in the present case did not value the debts due to him and, therefore, did not purport to show what his profits were but only what was due to him. In a commercial balance sheet debts are taken at their face value unless there is reason to suppose they will not be paid in full or at all. The assessee had not claimed that any part of the accrued interest will not be paid.

A number of cases were cited in which it has been held that interest accrued but not realised is not assessable. They are *Commissioner of Income Tax, Bengal* v. *Shaw Wallace and Company*; *The Secretary to the Board of Revenue* v. *Ar. Ar. Rm. Arunachlam Chettiar and Brothers*; *Messrs. Anglo Persian Oil Company, Ltd.* v. *Commissioner of Income Tax, Bengal*; *Narain Das Bhagwan Das* v. *Commissioner of Income Tax Punjab*; *The Board of Revenue* v. *Pydah Venkatachalapathy Garu* and *Lala Puran Mal* v. *The Commissioner of Income Tax Punjab*. Some of these cases were under the former Income Tax Act and some under the present Act, but none of them go to the length of deciding that unrealised interest may never be taken into account in computing the profits of a business. It would, I apprehend, be difficult to find a commercial balance sheet in this or any other country where such interest is not taken into account in ascertaining profits. It is the established practice of commercial houses and accountants to do so and the very nature of commercial profits necessitates it. It is no more true to say, in a commercial sense, that profits never include unrealised interest than it is to say that a cash receipt is necessarily a profit. In my view, therefore, there is no substance in the contention that unrealised interest is in no circumstances assessable to income tax, and, that being the case, the assessor was entitled to take such interest into account in ascertaining the assessee's profits unless the method of accounting regularly employed by the assessee is a method which ignores such interest.

MACPHERSON, J. :—The assessee, besides being a leading landholder conducts a money lending business upon which he has been

assessed to income-tax (as a Hindu undivided family). He made an application on the 28th November, 1931, requiring the Commissioner of Income Tax to refer to the High Court the question of law "Whether it is open to the Income Tax Officer to regard interest unrealised as taxable income" alleged to arise out of the appellate decision under Section 31 of the Income Tax Act, 1922, of the Assistant Commissioner, dated the 7th November 1931, and the Commissioner has made the present reference of 13th October, 1933 (not within sixty days but after nearly two years), purporting to be under Section 66 (2) of the Act formulating the question for opinion as: "Whether in the circumstances of this case, the assessee is liable to be taxed on his income from money-lending on the mixed cash and accrued basis which has been followed in his assessments of previous years?" (partly perhaps because their Lordships of the Judicial Committee deprecate the statement of a question of law in an abstract form and divorced from the facts of the particular case and partly for other reasons which will later appear) and expressing his own opinion that the answer is in the affirmative.

2. As is well-known, Section 66 (2) is indifferently framed (see also *Shiva Prasad Gupta* v. *Commissioner of Income Tax, United Provinces*). The Commissioner's statement of the case (which is to be read with the decision of the Income Tax Officer and of the Assistant Commissioner which are his Annexures *A* & *B*) also is obscure. A rather full exposition of the position is thus required as to ascertain what "the circumstances of the case" are.

3. In the years previous to the year of assessment which is 1931-32, the assessee submitted with his return of income two statements in support or explanation which are designated *A* and *B*. Statement *A* purported to show the interest which had accrued during the year on loans to borrowers from whom no realisation had been made during the year and against whom no suit had been filed, and statement *B* purported to show the realisations from those borrowers from whom full or part realisation had been made during the year. From the aggregate realisation shown in statement *B* the assessee deducted so much as had been shown as accrued interest in statement *A* furnished in previous years and so had then been taxed, and the aggregate of the balance so arrived at and of the accrued interest shown in the statement *A* for the year was the sum which he showed in his return as his profit for the year liable to income-tax. The profit so shown was

accepted as a correct computation under Section 13 after scrutiny of his books of account and other documents, the alterations being usually unimportant (except apparently in respect of 1930-31 where the interest accruing during the year on a debt under suit, was, as will appear later, also assessed); the method of accounting employed by the assessee during some fifteen years for computation of his profits is thus a combination of the cash (actual realisation) basis, and the accrued (otherwise called the mercantile or commercial) basis, or as it is expressed in the question propounded, the " mixed cash and accrued basis."

4. For the year 1931-32 however, the assessee filed only statement *B* and made the claim that he should be assessed on the cash basis only, the same deduction being made as in previous years, (that is to say, of interest realised in the year under assessment on which tax had in previous years been realised on the accrual basis as being included in the statement *A* of those years). The income from interest which he showed was Rs. 222-15-9 as against over Rs. 11,000 shown in 1930-31 (apart from Rs. 15,669-8-0 mentioned below) and over Rs. 30,000 shown in 1929-30.

5. The Income Tax Officer thereupon took action under Section 23 (2) and Section 22 (4) and the assessee caused to be produced the evidence and documents on which he relied in support of his return, and upon an examination of the assessee's accounts which admittedly exhibited no change of system from previous years, and his documents, the Income Tax Officer calculated therefrom " the assessable income " (or profits, as defined in *In re Spanish Prospecting Company*) of the year by taking the state of the business at the end of 1336 F. 1929-30 and at the end of 1337 F. 1930-31, and comparing the assets of the business at the two dates. Finding from Exhibit A the total investment up to the end of 1337 F. he deducted therefrom the aggregate of the total investment up to the end of 1336 F. and of the new loans advanced in 1337 F. and held as follows :—"In the income return the assessee showed only Rs. 222-15-9 as income from interest on the basis of actual realisation (cash basis), whereas the previous records show that the assessee's method of accountancy has all along been mercantile (accrued basis). The assessee's own accounts show that he calculates accrued interest in all cases in accordance with the stipulation in the bond and goes on raising the principal from year to year by the addition of accrued interest in the Lanna Bahi. So his method of accountancy is clearly mercantile which

has been rightly followed in the past and there is no justification to change the method of accountancy in the current year." There is thus a definite finding that the assessee follows the mercantile system of accounting and the last sentence is reminiscent of *Foster* v. *The Commissioner of Income Tax, Burma.* The assessee's petition of appeal has been printed but the order in appeal is only intelligible in the light of a further petition filed on the day before judgment was delivered. It is there pointed out that the argument on his behalf was that he did not keep his accounts on the commercial basis, his cash book showing only his cash receipts, and alternatively that if he was assessed on the accrued basis, he was at least entitled to deduction of Rs. 15,888-14-0 of which Rs. 15,669-8-0 was accrued interest of 1929-30 taxed in 1930-31 in the account of Ramprasad Singh while under suit in civil Court.

6. The decision in appeal sets out, first, that it was admitted that the computation of profits, if it was to be made on the accrued basis, was correct, subject to the deduction of the said sum of Rs. 15,669-3-0 on which tax had actually been deducted in the previous year, and subject to another deduction which is here immaterial. It then goes on to say that the assessee next claimed that he ought not to be assessed on the accrual basis at all. On this plea the Assistant Commissioner sets out that the assessee's money lending accounts consist of the personal accounts of his debtors wherein entry is made of the accrued interest from year to year and of the amount actually realised in each case, but neither the accrued nor the realised interest are totalled or accounted for in an interest account and no profit and loss is computed, and though there is a cash book in which the actual realisations are shown, there is no interest ledger, and he then states his conclusion thus :—" Clearly therefore the assessee has not computed his profit at all, and no particular method of accounting can be said to be regularly employed by him. The Income Tax Officer had therefore to make the computation of profit upon such basis and in such manner as the Income Tax Officer may determine and he decided to adopt the accrued basis which was also followed in previous year without objection on the part of the assessee". The Assistant Commissioner then negatived the contention on behalf of the assessee that the proviso to Section 13 of the Act did not entitle the Income Tax Officer to compute the profits on the accrual basis, the basis of which contention was that the accrued interest not actually received is not " income, profits or gains "

within the meaning of the Income Tax Act. What he failed to observe was that the Income Tax Officer had not proceeded under the proviso. In the result he maintained the computation of income and held it assessable subject to the deductions mentioned.

7. It was in consequence of the rejection of the contention mentioned that the application was, as already stated, made under Section 66 (2) to refer the question whether the Income Tax Officer was entitled to regard interest unrealised as taxable income. The argument on behalf of the assessee was that as the assessee does not, as the Assistant Commissioner found, employ any regular method of accountancy that can be accepted by the Department (and the accrual basis is such a method) for computing the profits of his money lending for purposes of income tax (this is a paraphrase of "no particular method of accounting can be said to be regularly employed by him") the substantive provision of Section 13 which is "income, profits and gains shall be computed, for the purposes of Sections 10, 11 and 12 in accordance with the method of accounting regularly employed by the assessee," does not apply and so the proviso to that section which is "Provided that, if no method of accounting has been regularly employed, or if the method employed is such that, in the opinion of the Income Tax Officer, the income, profits and gains cannot properly be deduced therefrom, then the computation shall be made upon such basis and in such manner as the Income Tax Officer may determine" must apply if anything does, and the assessee's profits cannot under the terms of the proviso itself, be computed on the accrual basis.

8. The point is now stated as being that even though in an assessment under the substantive portion of Section 13 the accrued basis may be adopted where the assessee has himself treated the accrued interest as income of the year under assessment, still as accrued interest is only notional income, the computation under the proviso to Section 13 must be of actual and not of notional income. In short the Income Tax Officer, it is contended, took the accrued (and unrealised) interest to be income, profits and gains of the year, whereas it is contended, it is not so in law unless the asseessee has so treated it in his accounts.

9. The Commissioner of Income Tax (as it happened, the same officer who was the Assistant Commissioner had become the Commissioner) being of opinion that the question of law as formulated by the assessee, did not cover all the facts of the case, substituted the question quoted above and referred it for decision purporting to do so under Section 66 (2).

10. Actually the question referred may be expanded as follows :—"Whether in the circumstances of the case the assessee is liable to income tax for 1931-32 on profits and gains from money-lending of 1930-31 on the aggregate of (*a*) the amount of interest accrued in 1930-31, when no interest has been realised and (*b*) the amount of interest realised in 1930-31 less the amount thereof previously assessed to income-tax."

11. The above statement of the facts expands what the Commissioner of Income Tax has said by the application of his Annexures A and B and the other papers.

12. In the statement of the case he then goes on to affirm that "as a matter of fact the assessee has been assessed neither on strictly cash basis nor on accrual basis." Computation of income in the year under assessment had he points out, been made on the same lines as had been adopted at the instance of the assessee himself in previous years; for certain reasons (which are set out but which are irrelevant) he had in 1931-32 claimed assessment on the cash basis under deduction of interest included in the cash realisation of the year where that interest had already been taxed on the accrual basis in the previous years. The Commissioner had in fact come to realise the inapplicability of some of the observations in the appellate judgment in which the computation of profit by the Income Tax Officer had been affirmed on a ground different from that on which it had been made. What he means appears to be that whatever theory applied, in fact computation had been on the same lines as in previous years as is indicated above, to wit, on the method of accounting (not a pure mercantile or a pure cash method of accounting but a mixture of these methods) which the assessee himself regularly employed and not under the proviso to Section 13: such are "the circumstances of the case", and the observations *obiter*, or even erroneous in the course of the appellate decision do not, it is implied, alter the fact that the assessment is under the substantive part of Section 13.

13. Then comes paragraph 6 in which apart from the affirmation above mentioned, he gives his own opinion on the case in which the High Court is consulted. It is that in fact the computation of the assessee's profits and gains has, as always hitherto, been made under the substantive portions of Sections 13, that is, in accordance with the method of accounting regularly employed by him. He bases this opinion on the following: the assessee had shown no ground for discarding his previous method of accounting;

no doubt the appellate finding that no regular (particular) system of accounting has been followed by the assessee is right in the sense that the assessee's books do not furnish a basis for an inference that either of the two well-known methods is followed, but it is not necessary that the method of accounting regularly followed be purely cash or purely mercantile, that is to say, it may be a mixture of the two systems and in fact the system which the assessee has actually adopted for computation of profits (to wit, the mixed system shown in the returns A and B) is a method of accountancy within the meaning of Section 13, and it is on that method that the computation of profit was made in previous years and in the year in controversy. His point is that in spite of observations in the appellate decision the computation has actually been made under the substantive part of Section 13. Finally he argues that even if (contrary to his view on the facts as stated by him) it is the proviso that is applicable in the case the assessment is nevertheless valid as being made on a basis and in a manner such as the Income Tax Officer is authorised to determine which it is implied, may be the accrual basis (with necessary modification). There is apparently no question that in the circumstances of this assessee, as disclosed by himself and his accountant the profit of the year may safely be computed as it has always been by himself as equal to the full interest (less remission shown) which has accrued within the year.

14. Thus the assessee's contention is that the legitimacy of the principles of computation applied by the assessee is a question of law and that the accrued interest debt due to him cannot be taxed as profits unless he treats it as such while the case for the Commissioner is that what has been held liable to income tax is not the unrealised accrued interest but the profit of the business computed on the assessee's own method of computation though it happens to be of the same amount (subject to the assessee's remissions and deductions mentioned) as the accrued interest. But the case stated implies that the assessee has treated the accrued interest as received by him (so that in the eye of the law it is a receipt) and (subject to deductions which are not in controversy) as profits of his business during the year. It would thus appear that the assessee's point is not here in controversy since in spite of the requisition of the assessee under Section 66 (2) the reference of the Commissioner cannot be said to include it; the reference definitely states the case as one in which a method of accounting though perhaps not a normal one, has been

regularly employed by the assessee himself from which moreover the profit of the business can properly be and has been deduced, and in such circumstances the proviso to Section 13 does not come in at all. The function of the High Court is to decide not the question set out in the application under Section 66 (2) but the question of law raised by the case stated, of which the question whether under the proviso to Section 13 the computation of profit can legally be on the basis of the accrued interest (with or without modification) is here not one.

15. Manifestly what happened is this. On considering the assessee's application under Section 66 (2) the Commissioner found himself as already indicated, in disagreement with the order of Assistant Commissioner where he had held in error of fact that the Income Tax Officer had applied the proviso to Section 13; two courses must have seemed open, either to review that order under Section 33 or to refer the larger question so that there might be tested the validity of the assessment whether under the substantive part of Section 13 or under the proviso thereto; if however he passed an order under Section 33, substituting reasons of his own for those of the Assistant Commissioner there was, until the first proviso to Section 66 (2) was inserted by Act XVIII of 1933, no provision for a reference under Section 66 (2) against his order; (though that proviso come into operation on the 11th September, the correction slip did not arrive until after the requisition had been considered); and thus the reference made on the 13th October, 1933, though nominally under Section 66 (2) is actually one which would be more appropriately be made under Section 66 (1) since though the case stated accepts the order under Section 31 in so far as that order dismissed the appeal, it rejects the grounds on which that order is made, and accepts the basis on which the Income Tax Officer computed the profit assessable (with modification in detail bringing it within the previous mixed cash and accrual basis); in fact the case stated is that the resultant computation of profit for the purpose of Section 10 is made on the method of accounting regularly employed by the assessee which though no doubt a mixed system, is one from which his profits can properly be and have been deduced.

16. I am accordingly constrained to the view that on the statement of the case referred for opinion it must be held that the computation of profit for assessment to income tax has as it stands, been genuinely made under the substantive part of Section 13 that is to say, on the method of accounting regularly employed by the

assessee and that accordingly no point of law arises thereon for decision under Section 66 (5). A reference back to the Commissioner under Section 66 (4) has not been suggested and it would probably not be helpful at this stage.

17. I may deal briefly with two incidental contentions for the assessee.

18. The first of these is that "in the circumstances of the case" the assessee in fact employs no method of accounting within the meaning of Section 13 so that a computation of profit thereon is not possible. But though it may be unscientific, a method of accounting is certainly regularly employed by him, which moreover he has himself utilised for over fifteen years to ascertain from it the sums on which he was in his own view liable to income tax as profit of his business.

19. The second contention is that the mere fact that hitherto the assessee has permitted himself to be assessed on sums, to wit, unrealised interest, which are really debts due to him and not profits of his business, does not involve a continuance of the method of accounting under which that was done with a consequent continuance of unwarranted taxation. That would be so but it is not the position here. What has to be ascertained is the profits and gains of his business as a whole, how much it has improved in the year and that is exactly what has been done. The assessee has indicated that in his view the accrued interest is a good asset at its face value and the computation of improvement has here been made on his own method of accounting in which he takes his unrealised interest as profit of the business. I agree with the view of AGARWALA, J., in this regard and particularly that the decision in *St. Lucia Usines and Estates Company Ltd.* v. *Colonial Treasurer of St. Lucia* and the arguments founded thereon are by no means favourable to the assessee in the circumstances of this case.

20. It is not necessary to express an opinion on the argument of Mr. Manohar Lal as to the proviso to Section 13 though it is attractive. His first claim which, as indicated, is that it does not apply, is good on the case stated, but as a last line of defence he was prepared to maintain that if the substantive part of Section 13 is held inappllicable and there is no method of accounting regularly employed by the assessee on which computation can be made or from which profits and gains can properly be deduced, the assessing authority is nevertheless entitled to utilise as the best rough and ready way available the method of accounting employed

even though *ex hypothesi* the " profits and gains cannot properly be deduced therefrom ".

21. The reference in the form in which it has been made, I would answer in the affimative. It is not implied that a reference is not possible on future materials in which the question originally submitted by the assessee might not properly arise for decision under Section 66 (5).

22. As the reference has not been made in a satisfactory manner, with resultant trouble to all concerned I would direct the parties to bear their own costs.

[IN THE HIGH COURT OF BOMBAY.]

INDIAN RADIO AND CABLE COMMUNICATIONS LTD.

v.

THE COMMISSIONER OF INCOME TAX, BOMBAY

Beaumont, C. J. and Rangnekar, J.

March 21, 1935.

BUSINESS EXPENDITURE—ONE COMPANY TAKING UP BUSINESS OF ANOTHER COMPANY AND AGREEING TO PAY SHARE OF PROFITS TO LATTER—ASSESSMENT OF FORMER COMPANY—AMOUNTS PAID TO VENDOR COMPANY, WHETHER ALLOWABLE DEDUCTION—INDIAN INCOME TAX ACT (XI OF 1922), SECTION 10 (2) (ix).

An English company which maintained radio and cable communications throughout the world entered into an agreement with the assessee, an Indian company by which the latter took over the Indian business of the English company together with all plant, machinery, instruments, etc. The assessee company agreed to pay a lump sum to the English company in respect of the costs of maintenance by the English company of its communication system throughout the world exclusive of India and in addition to this agreed also to pay in Bombay to the English Company one half of the net profits of the assessee company earned by it for each of its financial years. The question being whether the half share so paid to the English company was allowable in computing the taxable profits of the assessee company under Section 10 (2) (ix) of the Indian Income Tax Act :

Held, *that the half share thus paid was not in the nature of rent but was only a share of the profits and was not therefore an allowable deduction.*

PONDICHERRY RAILWAY CO., LTD. *v.* COMMISSIONER OF INCOME TAX, MADRAS [1931] (I.L.R. 54 MAD. 691; 59 I.A. 239; 132 I.C. 619; A.I.R. [1931] P.C. 165; 5 I.T.C. 368) *applied.*

Case stated by the Commissioner of Income Tax, Bombay under Section 66 (2) of the Indian Income Tax Act.

K. M. Munhsi with *Messrs. Craigie and Caroe,* for the assesseees.

The Advocate-General, for the Commissioner.

JUDGMENT.

BEAUMONT, C. J.—This is a case stated by the Commissioner of Income Tax under Section 66 (2) of the Indian Income Tax Act which raises a question "whether the half share of the net profits payable by the assessee company under Clause 5 of the agreement dated the 19th day of February 1935, *viz.*, Rs. 3,35,861 is a proper deduction to be allowed for the purpose of arriving at the amount on which this company should be assessed for the purposes of income tax and super tax within the meaning of Section 10 (2) (ix).

The sum in question is payable under the agreement referred to by the Commissioner and it is expressed to be a payment of half share of the net profits. The agreement is rather a long and complicated one made between the Imperial and International Communications, Ltd., which is an English company, and the assessee company. The arrangement is that the assessee company is to take over, putting it shortly, the Indian business of the English company, and to take over all plant, machinery instruments, apparatus etc., with it, and they are to pay a lump sum in respect of costs for maintenance by the English company of its communication system throughout the world exclusive of India. Then the material Clause is clause 5 (*b*) which provides that in addition to the lump sum mentioned above, the assessee company is to pay in Bombay to the English company one half of the net profits of the assessee company earned by it for each of its financial years. Then there is a provision as to how the half share in the net profits is to be calculated.

It is argued that the payment of the sum representing the half share in the net profits of the assessee company is really in the nature of rent payable under a lease for the property purchased. It is quite impossible to extract that meaning from the agreement. It is a perfectly plain agreement, from which it is clear that the assessee company acquired a certain business and certain assets and as consideration therefor agreed to pay a half share in the net profits to be ascertained as provided for in the agreement. Of course it may be that profits ascertained for the purposes of the agreement are not exactly the same as profits on which tax has to be paid. But that does not alter the fact that the English company is getting a share of the net profits. Therefore I agree with the Commissioner that the case is governed by the case of *The Pondicherry Railway Company* v. *The Commissioner of Income Tax, Madras* to which he refers. We are not of course concerned in this reference with any question between the assessee and the English company as to the ultimate liability to tax.

The question raised by the Commissioner must therefore be answered in the negative.

The assessee company to pay the costs of the Commissioner on the original side scale.

RANGNEKAR, J.—I agree.

[IN THE HIGH COURT OF BOMBAY.]

TATA HYDRO-ELECTRIC AGENCIES, LTD.

v.

COMMISSIONER OF INCOME TAX, BOMBAY.

Beaumont, C. J. and Rangnekar, J.

March 27, 1935.

BUSINESS EXPENDITURE—AGREEMENT TO PAY SHARE OF PROFITS TO THIRD PARTY IN CONSIDERATION OF SERVICES—AMOUNT PAID, WHETHER ALLOWABLE DEDUCTION—PROFITS, CALCULATION OF—INDIAN INCOME TAX ACT (XI OF 1922), SECTION 10 (2) (ix).

A company entered into an agreement with the assessee appointing the latter their managing agents and agreeing to pay

a commission of 10 per cent. of the profits to the latter and the assessee entered into an agreement with two other persons agreeing to pay two annas in the rupee each out of the commission which the assessee received. The question being whether in calculating the assessee's profits they were entitled to deduct the four annas in the rupee which they had thus to pay :

Held (*i*) *that the company was correctly assessed on the total amount of the commission received by them under the managing agency agreement without deducting from the said commission the four annas in the rupee paid by them.*

MACDONALD AND CO. v. COMMISSIONER OF INCOME TAX, BOMBAY [1935] (3 I.T.R. 459) *followed.*

(*ii*) *that the question whether the four annas share paid by them to third parties was expenditure incurred by them solely for the purpose of earning their commission was one of fact and there was no finding of fact on which the High Court could hold that the deduction was one falling within Section 10 (2) (ix).*

Case stated by the Commissioner of Income Tax, Bombay under Section 66 (2) of the Indian Income Tax Act. Civil Reference No. 12 of 1934.

The material facts are stated in the judgment. The questions referred were :

(1) Whether in the circumstances of the case and in view of the provisions of Sections 4 (1) and 10 of the Act, the assessee company has been correctly assessed on the total amount of Rs. 5,17,288 received by it as profits and gains of the business carried on by it as the Managing Agents of the Tata Power Co., Ltd.

(2) Whether under the provisions of Section 10 of the Act or under any other provisions thereof, the assessee company is entitled to have a deduction from the said profits and gains amounting to Rs. 5,17,288 to the extent of Rs. 1,29,322 paid by it to certain parties under the agreements Exhibits F. and G. on the ground that this latter amount was nothing but expenditure incurred solely for the purpose of earning the said profits or gains or on any other ground.

Engineer with *Wadia Ghandy & Co.* for the assessee.

The Advocate-General with the *Government Solicitor*, for the Crown.

JUDGMENT.

BEAUMONT. C. J.—This is a reference by the Commissioner of Income Tax under Section 66 (2) in which he raises two questions. The facts giving rise to the questions are simple. By an agreement made on the 24th September, 1919 Tata Sons Ltd., were appointed Agents for the Tata Power Co., Ltd., for 41 years on a commission of 10 per cent. profits plus an office allowance and there was power to assign the agreement and to assign any part of the commission. By an agreement of the 15th October 1926 Tata Sons Ltd, agreed to pay F. E. Dinshaw, Ltd., two annas in the rupee out of the commission which they received under the 1919 agreement, and four days later, that is on the 19th October, 1926, Tata Sons, Ltd., entered into a similar agreement with one Tilden Smith. On the 21st November, 1929, Tata Sons, Ltd., assigned their rights under the 1919 agreement to the present assessees subject to the agreement with F.E. Dinshaw, Ltd., and Tilden Smith. We are told that subsequently Tata Power Ltd., entered into direct agreement with the assessee for payment of 10 per cent. commission to them, and the assessees entered into a direct agreement with F. E. Dinshaw Ltd., and Tilden Smith for the payment of the two annas in the rupee to them. The first question raised is whether in the circumstances of the case the assessee company has been correctly assessed on the total amount of Rs. 5,17,288, received by it in respect of the 10 per cent. commission from Tata Power Ltd., as profits and gains of the business carried on by it as the Managing Agents of the Tata Power Co., Ltd., that is to say, whether the assessees have been correctly assessed on the whole 10 per cent. commission, or whether they are entitled to deduct four annas in the rupee which they have to pay to F.E. Dinshaw Ltd, and Tilden Smith. That part of the case seems to fall exactly within the decision of this court in *Macdonald & Co.* v. *Commissioner of Income Tax, Bombay* and we must follow that decision and answer the first question in the affirmative.

The Second question is whether the assessees can deduct the commission of two annas in the rupee which they have paid to F. E. Dinshaw Ltd. and Tilden Smith as being an expenditure not being in the nature of capital expenditure incurred solely for the purpose of earning commission, and thereby being a deduction authorised under Section 10 (2) Clause (ix) of the Income Tax Act. The question whether the expenditure

was incurred solely for the purpose of earning the profits or gains, *i.e.*, the commission is one of fact and there is no finding of fact on which we can hold that the deduction was one falling within that sub-section. That being so, the second question must be answered in the negative.

The assessee must pay the costs of this reference on the original side scale to be taxed by the Taxing Master.

RANGNEKAR J.—I agree.

[IN THE HIGH COURT OF BOMBAY.]

MRS. HIRABAI D. DESAI & SONS.

v.

THE COMMISSIONER OF INCOME TAX, BOMBAY.

Beaumont, C. J. and Rangnekar, J.

LIQUOR SHOPS—MODE OF ASSESSMENT—ASSESSEE KEEPING ACCOUNT NOT BY CASH RECEIVED BUT BY CHARGING MARKET PRICE FOR STOCK DIMINISHED PER DAY—VALUE OF ACCOUNTS—INCOME TAX OFFICER ADDING AMOUNT FOR KASRA—LEGALITY.

The assessee held a licence from Government to sell liquor at a shop. He entered in his accounts the amount of liquor purchased from the Government Depot and calculated the amount sold, not by the cash received but by charging the market price for the day for the amount by which the stock of liquor was diminished that day. The Income Tax Officer refused to accept this method of accounting as there was no fixed market price for liquor and made an assessment under the proviso to Section 13 adopting his own basis. He also added Rs. 42,797 in respect of kasar, *that is, selling by short measure, saying that it was a well known fact that all liquor sellers of the locality used to sell at short measure and that the assessee must be taken to have adopted this practice. On a reference by the Commissioner*: Held, (*i*) *that the Income Tax Officer was entitled in the circumstances to reject the assessee's system of accounting and to adopt a basis of his own but he ought to have shown in the assessment order the basis on which he arrived at the prices fixed by him*; (*ii*) *that the Income Tax Officer was not, however, entitled to add anything to the income of the assessee on account of* kasar *by charging the assessee with a criminal practice for which there was no evidence.*

CASE STATED BY THE COMMISSIONER OF INCOME TAX, BOMBAY UNDER SECTION 66 (3) OF THE INDIAN INCOME TAX ACT (Ref. No. 13 of 1934.)

Carden Noad with *U. L. Shah*, for the assessees.

The Advocate-General, for the Crown.

JUDGMENT.

BEAUMONT, C. J.—In this case the Income Tax Commissioner raised a question which he was directed by this Court to raise under Section 66 (3) of the Indian Income Tax Act, the question being "Whether the Income Tax Officer was, under the circumstances of the case, free to adopt the basis and manner of computing the income of the assessee, which he did adopt". The assessee holds a license from Government to sell liquor at a shop in Ahmedabad and the question is how she ought to be assessed in respect of the income of that liquor shop. The basis on which the accounts are kept is to enter the amount of liquor purchased, which can be easily checked as all liquor is purchased from the Government depot, and then to calculate the amount sold, not by the cash received, but by charging the market price for the day for the amount by which the stock of liquor was diminished that day. There is no fixed market price, and it becomes a question of fact, not always easy to answer, what was the price on any particular day. That method would not indicate the true income if the liquor had been sold at short measure, and it is suggested that the practice is not uncommon. The Income Tax Officer refused to accept that method of accounting, and I am not prepared to say that the Income Tax Officer was not entitled to reject that basis.

Having rejected that basis, he, under Section 13 of the Act, adopted his own basis, and he showed in his assessment order the prices at which he charged the liquor. I think he ought to have shown the basis on which he arrived at those prices. On the prices charged by him, the Income Tax Officer adds, to the income shown by the assessee a sum of Rs. 24,701. Then he also adds a sum of Rs. 42,767 in respect of what is called *kasar i.e.*, selling by short measure, and he says that it is a well-known fact that all liquor sellers in Ahmedabad do sell at short measure, and that the assessee must be taken to have adopted this practice. There is no evidence on record of any sale by short measure, and in my opinion the Income Tax Officer was not entitled to add

Rs. 42,767, to the assessee's income by charging her with a criminal practice for which there was no evidence. There was an appeal to the Assistant Commissioner who upheld the order of the Income Tax Officer. The matter was then referred to the Commissioner under Section 33, and he modified the assessment order. He added to the assessee's income shown in her return 10 per cent. on the amount of sale both for deficiency in the selling rate and *kasar*, and the figure he added came to Rs. 40,172 so that he reduced the figure of Rs. 67,488 (Rs. 24,701 plus Rs. 42,767) added by the Income Tax Officer on account of the two items to Rs. 40,172. He has not shown whether he accepted the same ratio which the Income Tax Officer adopted as between the deficiency in the selling rates and the *kasar*. In my opinion all that we can do is to answer the question raised by the Commissioner in the affirmative, but with this qualification that the Income Tax Officer was not entitled to add anything to the income of the assessee on account of *kasar*. With that answer the matter will have to go back to the Commissioner to ascertain the figure. There will be no order as to costs.

[IN THE HIGH COURT OF RANGOON.]

A. L. A. R. N. FIRM (BY THE OFFICIAL RECEIVER, M. K. R. RAMAN CHETTIYAR)

v.

THE COMMISSIONER OF INCOME TAX, BURMA.

Page, C.J., Mosley, J and Ba U., J.

February 25, 1935.

NOTICES—SERVICE OF NOTICE ON *Ad interim* RECEIVER OF ASSESSEES' ESTATE—VALIDITY—RECEIVER, WHETHER MANAGER, OR AGENT—INDIAN INCOME TAX ACT (XI OF 1922), SECTION 22 (2).

An ad interim *receiver was appointed for managing the assessees' estate on August 24, 1932 and on January 17, 1933, the appointment as receiver was made permanent. Meanwhile, on August 7, 1932, a notice was issued to the assessees under Section 34 and Section 22 (2) of the Indian Income Tax Act and it was served upon the receiver and accepted by him on behalf of the assessees. As the notice was not complied with an assessment was made under Section 23 (4). The assessees applied for cancellation*

of the assessment on the ground that they had not been duly served with the notice inasmuch as the receiver on whom the notice was served had not been confirmed in his office as receiver of the assessee's estate on the date of service of notice: On a reference by the Commissioner: Held, *that there were materials on which the Income Tax Officer could find that there was no sufficient cause for cancelling the assessment.*

Quære: *whether a receiver appointed by a Court* ad interim *or permanently as such and without more can be regarded in law as 'manager or agent' for purposes of service of notice.*

Case stated by the Commissioner of Income Tax, Burma under Section 66 (3), Indian Income Tax Act. (Civil Ref. No. 21 of 1934.)

P. K. Basu, for the assessees.

A. Eggar, for the Crown.

JUDGMENT.

PAGE, C.J.—The question propounded is; "whether, having regard to the admitted fact that at the time when a notice under Section 22 (2) of the Indian Income Tax Act was served upon the assessees M. K. R. Raman Chettiyar had not been confirmed in his office as receiver of the estate of A. L. A. R. N. Firm, there were any materials on which the Income Tax Officer or the Assistant Commissioner could find that there was no sufficient cause excusing the assessee from complying with the requirements of the law as prescribed in Section 27 of the Act."

The assessees are a firm of Chettiyar moneylenders carrying on business at Kyaungon.

On the 22nd August 1932 in Civil Miscellaneous No. 53 of 1932 the District Court of Rangoon ordered (1) that M.K.R. Raman Chettiyar should be appointed *ad interim* receiver of the firm's assets if and when a fidelity bond for Rs. 5,000 was executed by him, and (2) that the amount of security that would be required if his appointment as receiver was made permanent should be determined on the 20th September 1932. On the 23rd August 1932 the order appointing M.K.R. Raman Chettiyar interim receiver was drawn up. Under that order he was granted *inter alia* the power of managing the assessees' estate. On the 24th August 1932 M.K.R. Raman Chettiyar duly furnished security by executing the requisite fidelity bond and the order appointing him receiver was issued. On the January 17, 1933 the appointment of M.K.R. Raman Chettiyar as receiver was made permanent and the order of 23rd August was

confirmed. Meanwhile, on the 27th of August 1932, a notice was issued to the assessees under Section 34 and Section 22 (2) of the Income Tax Act and the notice was served upon and accepted by M.K.R. Raman Chettiyar on behalf of the assessee firm, he at that time being the receiver duly appointed to manage the estate of the assessees.

As the terms of the notice were not complied with an assessment was made on the firm under Section 23 (4) of the Act.

The assessees then applied under Section 27 that the assessment should be cancelled on the ground that they had not been duly served with the notice under Section 22 (2) as at the time when the notice was served on the firm through the receiver M.K.R. Raman Chettiyar's appointment as receiver had not been confirmed. The application was rejected.

In my opinion in the above circumstances the answer to the question propounded is in the affirmative. We refrain from considering or deciding whether a receiver appointed by a court *ad interim* or permanently as such and without more can be regarded in law as "manager or agent" within Order V, Rule 13 because (1) the question has not been referred in the case that has been stated (2), the assessees have never contended that M.K.R. Raman Chettiyar if he was duly appointed receiver before the notice of the 27th August was issued and served upon the firm, through him, was not the agent and manager of the assessee's business duly authorised to accept service of the notice on their behalf (3) the assessees, who throughout the proceedings in connection with the present assessment under Section 34 have acted by and through M. K. R. Raman Chettiyar have ratified and confirmed the action of M. K. R. Raman Chettiyar which he purported to take as the assessee's manager and agent.

The learned Government Advocate is entitled to costs, Advocate's fee eight gold mohurs.

MOSLEY, J.—I agree.

BA U, J.—I agree.

[IN THE RANGOON HIGH COURT.]

ADAM HAJI DAWOOD AND CO., LTD.
v.
COMMISSIONER OF INCOME TAX, BURMA.

Sir Arthur Page, C. J. and Ba U, J.

July 1, 1935.

REFUND—DIVIDENDS—DEDUCTION OF TAX AT SOURCE AT HIGHER RATE—APPLICATION FOR REFUND—LIMITATION—POWER OF COURT TO EXTEND TIME—NECESSITY OF AMENDMENT OF ACT—REFERENCE FROM ORDER RELATING TO REFUND—MAINTAINABILITY—INDIAN INCOME TAX ACT (XI OF 1922), SECTIONS 48, 50 AND 66 (2) AND (3)—SPECIFIC RELIEF ACT (I OF 1877), SECTION 45.

Section 66 (3) of the Indian Income Tax Act is controlled by Section 66 (2) and inasmuch as 66 (2) does not empower an assessee to require the Commissioner of Income Tax to state a case to the High Court in respect of a question of law arising out of an order on an application for refund under Section 48, the assessee is not entitled to apply to the High Court under Section 66 (2) to require the Commissioner to state a case in respect of an order on an application for refund.

Though it may be impossible for an assessee to ascertain whether or not he is entitled to a refund under Section 48 (1) until an assessment has been made upon him the court has no power to extend the period prescribed by section 50 for making an application for refund on this ground, as the legislature has not invested the Court with any such power with regard to applications under Section 48 (1), though it has expressly given such power in respect of applications under Section 49.

The Court cannot act under Section 45 of the Specific Relief Act in respect of a question arising under Section 48 (1), as a specific remedy is available to the assessee under Section 50-A

Cases referred to:

COMMISSIONER OF INCOME TAX, BURMA *v.* C. P. L. E. FIRM [1934] (2 I.T.R. 132; 150 I.C. 408; 12 Rang. 322) (F.B).

N. A. S. V. VENKATACHALAM CHETTIAR *v.* COMMISSIONER OF INCOME TAX, MADRAS [1935] (3 I. T. R. 55; 8 I. T. C. 74; 156 I.C. 64; 58 Mad. 367; 68 M.L.J. 227) (S.B.)

TATA HYDRO ELECTRIC AGENCY LTD., *v.* COMMISSIONER OF INCOME TAX, BOMBAY, [1934] (2 I. T. R. 103; 1934 BOM. 62; 150 I.C. 52; 58 BOM. 361; 36 BOM. L.R. 23).

V. E. A. CHETTIAR FIRM *v.* COMMISSIONER OF INCOME TAX, [1930] (A.I.R. 1930 RANG. 37; 121 I.C. 769; 7 RANG. 581: 3 I.T.C. 436.)

Application (C. Mis. Appl. No. 36 of 1935) under Section 66 (3) of the Indian Income Tax Act, (XI of 1922), to require the Commissioner of Income Tax, Burma, to state a case.

D. J. Daniel for the applicant.

A. Eggar for the respondent.

PAGE, C. J.—In this case the assessee, a limited company carrying on business under the style of Adamjee Hajee Dawood and Co., Ltd., has applied to the Court under Section 66 (3), Income Tax Act, for an order requiring the Commissioner of Income Tax to state a case and refer the following question for determination by the High Court:

"In a case in which the assessment upon the total income of the assessee is made more than a year after the last day of the year in which the tax on the profits of a company was recovered, and after the last day of the financial year commencing after the expiry of the previous year as defined in Clause 11, Section 2, in which the income arose on which the tax was recovered, does Section 60, Income Tax Act, 1922, preclude a claim for a refund of income tax under Section 48 (1) if made after the expiration of the period mentioned in Section 50 when it is preferred before the assessment upon the total income of the assessee was made?"

The material facts are few and not in dispute. For the year of assessment, 1932-33, the Income Tax Officer found that the net loss suffered by the assessee was Rs. 11,50,343 and declared the company to be non-assessable to income-tax in respect of that year. That order was made on 22nd June 1934. It appears that the assessee was entitled to dividends in respect of shares which it held in certain companies; and that income tax upon these dividends had been deducted at the source at the rate at which the company's profits and gains were assessable. Now, Section 48 (1) of the Act runs as follows:

"If a shareholder in a company who has received any dividend therefrom satisfies the Income Tax Officer or other authority

appointed by the Governor-General-in-Council in this behalf that the rate of income-tax applicable to the profits or gains of the company at the time of the declaration of such dividend is greater than the rate applicable to his total income of the year in which such dividend was declared or that his total income in such year is below the minimum chargeable with income-tax he shall, on production of the certificate received by him under the provisions of Section 20, be entitled to a refund on the amount of such dividend (including the amount of the tax thereon) calculated at the difference between those rates or at the rate applicable to the profits and gains of the company at the time of the declaration of such dividend, as the case may be."

It is apparent from the assessment that the income chargeable to income-tax in the hands of the assessee which was nil fell to be assessed under Section 48 (1) at a lower rate than that at which the dividends were chargeable at source in the hands of the company and the assessee contends that in fact the Crown has obtained income-tax upon the assessee's dividends at a rate higher than that to which the Crown was entitled, thereby diminishing the amount of the dividends received by the assessee. The first answer to the case presented on behalf of the assessee is that Section 66 (3) Income Tax Act, is controlled by Section 66 (2); and under Section 66 (2) an assessee is not entitled to require the Commissioner to a state a question of law arising out of an order under Section 48. Section 60 (3) therefore does not entitle the assessee to apply to the Court to require the Commissioner to state a case and refer the question which the assessee seeks to have answered. That in itself is sufficient to dispose of the present application. The learned Government Advocate on behalf of the Crown however pointed out that there were further objections to the grant of an order in the nature of a mandamus to the Commissioner of Income Tax in the circumstances of the present case. He submitted that, if the facts of the case did not bring the present application within Section 66 (3) of the Act, it was not open to the assessee to have recourse to Section 45, Specific Relief Act, by reason of the provisions of Sections 50 and 50-A which are to the following effect:

"50. No claim to any refund of income tax under this Chapter shall be allowed, unless it is made within one year from the last day of the year in which the tax was recovered or before the last day of the financial year commencing after the expiry of

the "previous year" as defined in Clause (11) Section 2 in which the income arose on which the tax was recovered, whichever period may expire later; provided that a claim to refund under Section 49 may be admitted after the period of limitation herein prescribed, when the applicant satisfies the Commissioner, or Assistant Commissioner of Income Tax specifically empowered in this behalf by the Central Board of Revenue, that he had sufficient cause for not making the claim within such period.

50-A. (1) Any person objecting to a refusal of an Income Tax Officer to allow a claim to a refund under Section 48 or 48-A or Section 49 or to the amount of the refund made in any such case, may appeal to the Assistant Commissioner. (2) The appeal shall be presented within thirty days of the date on which the refusal of the refund or the amount of the refund allowed was communicated to the appellant. (3) The appeal shall be made in the prescribed from and shall be verified in the prescribed manner. (4) The Assistant Commissioner may, after giving the appellant an opportunity of being heard, pass such orders as he thinks fit."

Now, it is common ground that the application for a refund in the present case was made on 12th June, 1933, and that at that date the application was time-barred under Section 50. In these circumstances the learned advocate for the assessee has invited the Court to treat the appeal of 13th July, 1934, to the Assistant Commissioner from the order of assessment of 22nd June, 1934, as an application for a refund; but if the Court were to do so the result would be that the application for refund would be more completely barred than it would be if it had been made on 12th June, 1933. The learned advocate for the assessee further contended that as it is in fact impossible for an assessee to ascertain whether or not he is entitled to a refund under Section 48 (1) until the assessment has been made upon him, an assessee ought not to be held bound to present his application for a refund within the period limited by Section 50 where the assessment has not been made until after the expiry of that period. That may be so, but the remedy lies not with the Courts but with the legislature. The Commissioner of Income Tax, on 12th July, 1934, rejected the application for a refund which had been made to him on 12th June, 1933, upon the ground that it was time barred under Section 50, and that there was no power given to him under the Act to extend the period prescribed in that section. In my opinion in so holding the Commissioner was plainly right. Indeed, it appears to me to be apparent that the view he took was correct from the

terms of Section 50 itself. It is to be observed that in Section 50 an extension of the time within which an application may be made for relief in respect of United Kingdom income tax under Section 49, is permitted; but although it is clear that the legislature had both Sections 48 and 49 in mind when Section 50 was enacted it deliberately refrained from permitting any extension of the time within which the application for a refund should be made in respect of a claim under Section 48. In my opinion upon that ground also the present application must fail.

The learned Government Advocate also contended that in any event the present application must fail both because it does not fall within Section 66 (3) and because a specific and adequate remedy was available to the assessee under Section 50-A, and for that reason he was precluded from taking advantage of Section 45, Specific Relief Act: *V.E.A. Chettiyar Firm* v. *Commissioner of Income tax, Burma*; *Commissioner of Income Tax, Burma* v. *C.P.L.E. Firm*; *N.A.S.V. Venkatachalam Chettiyar* v. *Commissioner of Income Tax, Madras* and *Tata Hydro Electric Agency, Ltd.* v. *Commissioner of Income Tax, Bombay.* For these reasons, in my opinion the rule must be discharged and the application for a mandamus dismissed with costs ten gold mohurs. It is no part of the function of this Court to express any opinion as to whether the Government should make a refund in whole or in part *ex gratia* and we express no opinion about it.

BA U., J.—I agree.

[IN THE LAHORE HIGH COURT]

HAKIM RAM PRASAD, *In re.*

Sir Douglas Young, C. J. and Monroe, J.

December 12, 1935.

BUSINESS EXPENDITURE—CINEMA PROPRIETOR PAYING ANNUAL SUMS FOR USE OF ELECTRIC APPARATUS—SUMS PAID, WHETHER RENT OR CAPITAL EXPENDITURE—CONSTRUCTION OF AGREEMENT—INDIAN INCOME TAX ACT (XI OF 1922), SECTION 10 (2) (ix)—INCOME TAX RULES, RULE 8, CLAUSE 3 (*b*).

The assessee who owned a cinema installed an Electric Company's Projector equipment in 1930 under an agreement which provided that the assessee should have the use of the projector for 10 years, that he should keep the equipment in order, that the company should make the necessary repairs, and that at the expiry of the agreement the machine was to be handed back to the company.

these are the essential parts of the agreement. The payments were to be in the first year, of Rs. 41,856, and thereafter payment by the assessee to the company of Rs. 4,800 a year, in addition to an initial payment of Rs. 10,950. For the year under assessment 1932-33 the cinema made a net profit, according to the Commissioner, of Rs. 54,000 odd. This was arrived at, however, without taking into consideration the payment of Rs. 41,000 odd for the first year to the projector company. The assessee objected. He claimed that this payment was in the nature of rent and therefore should be deducted from his profits. The Commissioner on the other hand contends that this payment was in the nature of capital and is therefore not deductible from the profits for that particular year.

The question that we are asked to decide is "was there any material upon which the Income Tax Officer could find that part of the payment of Rs. 52,806, for "Talkies" apparatus under the agreement described in the case was in the nature of capital expenditure and not allowable in the terms of Section 10. There is a further question which we are asked to decide as to whether item 3 (*b*) of Rule 8 is applicable to the cinematograph apparatus described in the case, that is the projector used in the cinema theatre electrical apparatus or not.

We have come to the conclusion that we have no material before us either to decide the first question or the second.

On the face of the agreement, the agreement is clearly an ordinary renting agreement. The property in the apparatus leased remains at all material times the property of the lessor company. The exhibitor *i.e.*, the assessee, has to keep the equipment in good order and repair. It has to be handed over at the end of ten years to the lessor. This would clearly be an ordinary agreement for lease. We agree with Mr. Jagan Nath Aggarwal, who appears for the Commissioner, that there are cases where the sum paid nominally for rent could be dissected and a conclusion arrived at whether the payment, or what portion of it, is capital or revenue. But to arrive at a conclusion of that nature, the Court must be in possession of the facts. The only evidence before us is this agreement which, as we have pointed out, *prima facie* shows that there was no difference between this agreement for lease and any other agrement for lease. The mere fact that the lessor takes, as in this case, half the total rent in one year, the rest of the rent being spread over nine years, gives us no information upon which we can come to any conclusion as to whether the first payment is in

the nature of a premium or merely, as it might well be, a payment of such a nature that would at least take away any risk of loss to the lessor company. For example, before a decision could be arrived at in this case, it would be very necessary to know what is the total value of the leased machinery installed in this theatre. If for example, it were proved that the lessee was paying in the course of ten years the total value of the machinery and that the machinery would be of no value at the end of ten years, the Court could probably come to a decision that the whole expenditure over the ten years was in the nature of capital, except such amount which would have to be allowed as interest. On the other hand, it may very well be that the total payment over the ten years is only a fair rent for the machinery during that period, and that further the value of the machinery at the end of ten years may be quite a substantial amount. The learned Commissioner has apparently taken his facts on this point entirely from his own imagination. He says that capital payment is completed within the first year. We do not know that and unless the Commissioner had evidence which is not before us he could not possibly have known it. He also says that the exhibitor at the end of ten years will give up the then useless asset. Again, we do not know what evidence the Commissioner had before him upon this matter, but there is absolutely none before us. Again he says "at a date when it is anticipated that it will have no further useful life (which I would state as fact is expected to end long before the term of ten years)". There is not only no evidence on this before us but strong evidence to the contrary. If it has no useful life before ten years have passed, the agreement itself would be sheer waste paper.

We are clear therefore that in this reference there are no facts upon which we can come to any conclusion upon the matter.

The same applies to the second question put to us. The only fact which is placed before us is that the article is a projector. There is no information as to what machinery, if any, is in the projector. Does it contain a dynamo or a converter? It may be the Income Tax Commissioner knows, but we certainly do not. In a case of this sort, detailed description of the machinery ought to be put before the Court accompanied by a blue print, plan, or something of the nature.

We, therefore, answer the reference as follows :—

There is no material upon which the Income Tax Officer could find that the payment of Rs. 52,806 or part of it was in the nature of capital expenditure. There is no material either to enable us to answer the second question. We allow the costs to the assessee. Rs. 100, deposit will be refunded.

Order accordingly.

[IN THE PATNA HIGH COURT.]

RAMKINKAR BANERJI

v.

COMMISSIONER OF INCOME TAX, BIHAR AND ORISSA.

Courtney-Terrell, C. J., and Mohammad Noor, J.

November 27, 1935.

COLLIERY—ACQUISITION OF SUPERIOR LANDLORD'S RIGHT BY ASSESSEE'S WIFE—PAYMENT OF ROYALTY TO WIFE—DEDUCTION—NO PRESUMPTION THAT WIFE IS ONLY A BENAMIDAR.

Where the assessee who had an interest in a colliery paid a sum of Rs. 15,353 odd as royalty to his wife who had acquired the interest of the superior landlord but the income tax authorities refused to allow him to deduct this amount from his income on the ground that there was no evidence to show that the superior landlord's rights were acquired by his wife out of her own funds: Held, *that in the absence of evidence to the contrary, the wife must be presumed to have acquired the rights with her own funds and to be the owner thereof, and the assessee was entitled to have the amount deducted.*

Case stated under Section 66 (3) of the Indian Income Tax Act (Act XI of 1922) by the Commissioner of Income Tax, Bihar and Orissa.

The necessary facts are stated in the judgment.

S. M. Gupta and *R. S. Chatterjee*, for the assessee.

Manohar Lal, for the Commissioner.

MOHAMMAD NOOR, J.—Under the orders of this Court, dated August 20, 1934, the Commissioner of Income Tax has under Section 66 (3) of the Income Tax Act submitted a statement of the case for the orders of this Court. The proposition of law which, as ordered by this Court, he has submitted is "whether upon the facts as found by the lower Appellate Court (meaning thereby the Assistant Commissioner) the assessee is entitled to a deduction of

Rs. 15,352 as claimed by him". The facts as stated by the Commissioner are these.

The assessee has an interest in the Sitalpur Colliery which was being worked by Mesrs. Ojha & Co. who paid him in the year in question Rs. 15,408-14-0 as royalty. The assessee did not include this income in the return. The Income Tax Officer somehow or other came to know of this income and called upon the assessee to show cause why a penalty should not be imposed upon him under Section 28 of the Indian Income Tax Act for concealing this income. Thereupon the assessee appeared and stated that he did not in fact get any income inasmuch as he had paid Rs. 15,353 as royalty to the superior landlord who, admittedly for some time, was Mr. L.A. Creet, but whose right to receive the royalty had been acquired by Saibalini Debi, the wife of the assessee. The assessee also gave some other figures showing a loss of Rs. 184-11-3 on his colliery income. The Income Tax Officer seems to have accepted the other figures of the assessee but apparently treating the lady to be his benamidar refused to allow him to deduct Rs. 15,353 for the royalty and included this amount for the purposes of the assessment. The assessee appealed to the Assistant Commissioner of Income Tax who upheld the order of the Income Tax Officer but allowed a deduction of Rs. 4,000 which the lady had to pay to her own superior landlord. The Income Tax Commissioner having refused to refer the question of law stated above to this Court, the assessee came up to this Court and obtained the order above referred to.

Now the contention on behalf of the assessee before us has been that as it was not disputed by the department that if in fact Rs. 15,353 was paid as royalty, it was not open to the Income Tax Officer or to the Assistant Commissioner to refuse to deduct this amount on the ground that there was no evidence to show that the lady acquired the right of Mr. Creet from her own stridhan funds. Mr. Gupta contends that having shown the payment of royalty, the duty of the assessee ended. If the department wanted to refuse deduction of this amount on the ground that the lady was a benamidar, they could only do so on some evidence and not on the ground that there was no evidence that the lady was the real owner. The facts found by the Assistant Commissioner and his reasons summarised by the Commissioner are :

(*a*) That the right by virtue of which the payment of Rs. 15,353 was made stands in the name of S. Devi, the assessee's wife;

(*b*) That it was not seriously contended that she acquired this right with her stridhan nor was any evidence to that effect produced, and

(*c*) That in the absence of any evidence to the contrary, it was reasonable to presume that the right in question was acquired by the assessee as head of the undivided family in the name of his wife.

There being, therefore, no dispute that the property stands in the name of the lady, she must be taken to be the owner of it unless there is any evidence to show that she is a benamidar. Nos. (*b*) and (*c*) are not strictly speaking findings of fact but are reasons given by the Assistant Commissioner for holding that the real owner was the assessee. They are based upon no evidence whatsoever. There is no presumption that a property standing in the name of a married Hindu lady does in fact belong to her husband. The ordinary presumption of law is that the apparent state of affairs is real unless the contrary is proved. The absence of evidence one way or the other did not under the law justify the Assistant Commissioner in drawing an inference that the lady was a benamidar of her husband. If the Assistant Commissioner had disbelieved the payment of the money, much would have been said in favour of the view that it was a finding of fact but in this case the payment is not disputed. What the Assistant Commissioner has found is this, that the payment was to himself because the lady in whose name the payment has been made was a benamidar. For coming to this finding some evidence was essential, which, in my opinion, was wanting in this case.

I would, therefore, answer the question of law referred to this Court in the affirmative.

The petitioner will be entitled to a refund of his deposit and also to his costs incurred in this Court; hearing fee ten gold mohurs.

COURTNEY-TERREL, C. J.—I agree.

Answered in the affirmative.

[IN THE LAHORE HIGH COURT.]

VIR BHAN, BANSI LAL

v.

COMMISSIONER OF INCOME TAX, PUNJAB.

Sir James Addison, J., and Abdur Rashid J.

January 24, 1936.

NOTICE—NOTICE FOR ASSESSMENT OF INCOME WHICH HAS ESCAPED—CONTENTS—OMISSION TO ASSESS THINKING ASSESSEE HAS INCURRED LOSS—RE-ASSESSMENT—LEGALITY—INCOME TAX ACT (XI of 1922), SECTIONS 22 AND 34.

The requirements of a notice under Section 22 (2) of the Income Tax Act may be included in a notice under Section 34. It is not necessary to issue a separate notice under Section 22 (2) also when a notice under Section 34 is issued.

When an Income Tax Officer finds that the assessee had in fact books of account and that they were not produced in accordance with a notice under Section 22 (4) of the Act, he is entitled to make a best judgment assessment under Section 23 (4).

Where an Income Tax Officer omitted to make an assessment on the assessee believing that the assessee had incurred a loss in his business but subsequently discovered that the assessee had incurred no loss but in fact made some profit : Held, *that he was entitled to take proceedings under Section 34 of the Act.*

Case referred to:

MADAN MOHAN *v.* COMMISSIONER OF INCOME TAX, PUNJAB AND N.W.F.P. [1935] (I.L.R. 16 Lah. 937 ; 3 I.T.R. 438.)

Case stated under Section 66 (2) of the Indian Income Tax Act (XI of 1922) by the Commissioner of Income Tax, Punjab, North West Frontier and Delhi Provinces, Lahore. The necessary facts are stated in the judgment.

Kirpa Ram Bajaj, for the assessee.

J. N. Aggarwal, for the Commissioner.

ORDER.—Under Section 66 of the Indian Income Tax Act the following three questions have been referred to this Court by the Commissioner of Income Tax, Punjab, namely :—

(1) Whether Section 34 of the Income Tax Act was applicable to the case or not?

(2) Whether the notice under Section 34 issued by the Income Tax Officer was a legal notice within the meaning of Section 34?

(3) Whether, in the circumstances of the case, the assessment was rightly made under Section 23 (4)?

The assessees are a Hindu undivided family consisting of two brothers Vir Bhan and Bansi Lal. They were assessed to various sums on their income up to the year 1930-31 but in 1931-32 they were not assessed to income tax on the claim that their business had been running at a loss. In January 1932, the Income Tax Officer received certain information which led him to serve a notice upon the assessees under Section 34 of the Act, for the year 1931-32. This was served within time. The assessees put in a return of income on the 16th May, 1933, showing a loss of Rs. 5,407. The accounts were carefully gone into, serious omissions and discrepancies were discovered and it was found that there were certain other books besides the cash book and ledger produced by the assessees which had not been produced for examination. A fresh notice under Section 22 (4) was therefore served on the assessees calling for certain *bahis etc.* On the 12th June, 1933, Vir Bhan appeared and stated that no *lekha bahis* were kept for the money lending business, that is, he denied the existence of such *bahis.* Thereafter he put in a revised return showing a profit of Rs. 5,856-3-6 instead of a loss of Rs. 5,407. This return was also found to be incorrect and not to be in accordance with those books which were produced, certain omissions being discovered and other defects noted. Another notice was therefore issued under Section 22 (4) to produce certain other account books, promissory notes, *hundis*, bonds, mortgage deeds and sale deeds, *etc.* On the facts which came to his notice the Income Tax Officer held that the *lekha bahis* specified in the notice were being withheld while the bonds, promissory notes and mortgage deeds were also not produced. A final notice under Section 22 (4) was issued to produce the necessary accounts and documents on the 8th June, 1934, when Vir Bhan appeared and denied the existence of those books and declined to comply with the notice. The Income Tax Officer therefore held the assessees to be liable to assessment under the provisions of Section 22 (4) and he proceeded so to assess them.

The contention raised in the first question was not seriously pressed before us and is decided by the Special Bench case, *Madan Mohan* v. *Commissioner of Income Tax, Punjab.* There is no doubt that Section 34 of the Act is applicable in the circumtances mentioned and our reply to this question is in the affirmative.

The reply to question No. 2 is contained in Section 34 itself. What was contended on behalf of the assessee was that, besides a notice under Section 34, there should also be a regular notice as provided by Section 22 (2) of the Act, but Section 34 itself mentions that the notice under it may contain all or any of the requirements which may be included in the notice under Section 22 (2) and this means obviously that another notice under Section 22 (2) is not necessary. Our reply to the second question is therefore also in the affirmative.

As regards the third question the answer must also be in the affirmative. On the facts found there was a default. It was held by a Division Bench of the Patna High Court in 5 I. T. C. 389 that where the Income Tax Officer came to the conclusion that the assessee had in fact books of account, which were not produced in accordance with a notice under Section 22 (4) of the Act, he was entitled to make an assessment to the best of his judgment under Section 23 (4). Apart from that it is obvious that in the present case other documents have been withheld. This is a case where there has been deliberate misrepresentation on the part of the assessees to the income tax authorities. We further direct that the assessees pay the costs of the Income Tax Commissioner.

Order accordingly.

[IN THE HIGH COURT OF LAHORE.]

DHANIRAM DHARAM PAL

v.

COMMISSIONER OF INCOME TAX, PUNJAB & N. W. F. P.

Sir James Addison, J., and Abdul Rashid, J.

January 24, 1936.

INCOME TAX—RETURN FILED AFTER ASSESSMENT BUT BEFORE NOTICE OF DEMAND—VALIDITY—INDIAN INCOME TAX ACT (XI OF 1922), SECTIONS 22 (3) AND 29.

A return filed after an assessment is made but before a notice of demand is served on the assessee under Section 29, is not a valid return.

Case referred under Section 66 (2) of the Indian Income Tax Act (XI of 1922), by the Commissioner of Income Tax, Punjab and N.W.F. and Delhi Provinces, Lahore.

The necessary facts appear in the judgment.

Kirpa Ram Bajaj, for the assessee.

J. N. Aggarwal, for the Commissioner.

ORDER.

The one question of law referred by the Commissioner of Income Tax in this case is :—

"What is the legal effect of the return being furnished before the service of the demand notice?"

A return is due under Section 22 (2) within such period, not being less than thirty days, as may be specified in the notice. As a concession Section 22 (3) allows a person, who has not furnished a return within the time allowed by sub-Section (2), to furnish a return at any time before the assessment is made and a return so made is to be deemed to be a return made in due time. In the present case the return was not made until after the assessment order was made, but was made before the notice of the demand specified by Section 29 was served upon the assessee by the Income Tax Officer. It seems to us obvious that the return was not made within the time allowed by Section 22 (3) as the assessment was made within the meaning of Section 23 before the return was put in. It is true that the assessee contrived to put it in before the notice of demand was served upon him under Section 29 but this makes no difference. Our answer to the question is that the return furnished after the assessment order was made but before the service of the demand notice was not a valid return. We make no order as to costs.

[IN THE LAHORE HIGH COURT.]

THE PROBYNABAD STUD FARM, *In re.*

Sir James Addison, Ag. C. J., and Din Mohammad, J.

July 9, 1935.

and

Jai Lal and Skemp, JJ.

December 12, 1934.

TRUST—STUD FARM FOR IMPROVEMENT OF HORSE BREEDING AND SUPPLYING REMOUNTS TO ARMY—INDEFINITENESS OF OBJECTS—DISBURSEMENTS LEFT TO TRUSTEE'S DISCRETION—NO PART DEFINITELY SET APART FOR CHARITABLE PURPOSES—NO EXEMPTION FROM INCOME TAX—LIABILITY OF TRUSTEE FOR TAX—

ASSESSEE,' MEANING OF—AGRICULTURAL INCOME—'DHARAT' (WEIGHING CHARGES) LEVIED BY LANDLORD FROM TENANTS—WHETHER EXEMPT—INDIAN INCOME TAX ACT (XI OF 1922), SECTIONS 2 (1) (*b*), 3, 4 (2) (*i*).

A Stud Farm was founded by a military officer (Colonel Probyn) in 1864 by obtaining from the Government a grant of lands and with the help of some other funds and savings from certain subscriptions. The income from the farm, securities and other sources was used to finance the breeding of horses and the control of the farm was in the hands of the Officer Commanding Probyn's Horse for the time being as trustee. The main object of the Stud Farm was originally to supply remounts for the regiment and to improve horse-breeding in India. The majority of the horses bred were supplied to the Army Department on payment and stallions and brood mares were also imported. Stock unsuitable for remounts was sold publicly. There was no deed of trust defining the objects of the trust and it appeared that the Officer Commanding Probyn's Horse had a discretion to make such disbursements as he thought fit and the accounts showed that Rs. 1,74,518 was once paid as bonus to the regiment, Rs. 23,113 was spent for giving farewell to the Commander-in-Chief, Rs. 698 for a wedding party and so on. On a reference by the Commissioner:

Held, (*1*) *that the Officer Commanding Probyn's Horse could rightly be assessed to income-tax as the 'assessee' under the Indian Income Tax Act, as he was the person in actual receipt and control of the income of the Farm* ; (*2*) *that it was clear from the nature of the disbursements that the property of the Farm was not held in trust wholly for any charitable purposes and that even a part of the property had not been set aside exclusively for any such purposes, and further, as the Officer Commanding had a discretion as to disbursements, the income of the trust was not entitled to the benefit of the exemption provided for in Section 4 (3) (i) of the Indian Income Tax Act.*

Held also, *that income from* dharat, *i.e., weighing charges which were levied by the assessee from the tenants of the land in addition to the rent received from them under the agreements entered into with the tenants was agricultural income and was exempt from income-tax.*

Cases referred to:

ALT v. STRATHEDEN AND LORD CAMPBELL; RE STRATHEDEN AND CAMPBELL [1894] (3 Ch. D. 265; 63 L.J. Ch. 1872; 71 L. T. 225).

GOOD, *In re.*, HARRINGTON v. WATTS [1905] (2 Ch. D. 60; 74 L.J. Ch. 512; 92 L.T. 796).

HOTZ TRUST, *In re* [1930] (I.L.R. 11 Lah. 724; 5 I.T.C. 8; A.I.R. 1930 Lah. 929).

MORICE v. DURHAM [1805] (32 E.R. 947; 10 Ves. 522).

MOORE v. SOMERSET, *Re*, DONALD [1909] (2 Ch. D. 410; 78 L.J. Ch. 761; 101 L.T. 377).

MUHAMMAD IBRAHIM RAZA MALAK v. COMMISSIONER OF INCOME TAX, NAGPUR [1930] (129 I.C. 879; A.I.R. 1930 P.C. 226; 26 N.L.R. 256; 32 Bom. L.R. 1538; 35 C.W.N. 36).

PEMSEL v. SPECIAL COMMISSIONER OF INCOME TAX [1891] (1891 A.C. 531; 61 L.J.Q.B. 265; 3 Tax Cas. 53).

R. v. SPECIAL COMMISSIONERS OF INCOME TAX, *Ex parte* BANK'S TRUSTEES [1922] (38 T.L.R. 256; 8 Tax Cas. 286).

SRI THAKURJI MAHARAJ v. SUKHDEO SINGH [1920] (I.L.R. 42 All. 395; 58 I.C. 583).

SUSANNA BARKER *In re*: SHERRINGTON v. DEAN OF ST. PAUL'S CATHEDRAL [1909] (25 T.L.R. 753).

THE TRIBUNE, *In re* [1935] (1935 I.T.R. 246; 8 I.T.C. 353).

Case stated by the Commissioner of Income Tax, Punjab and N.W.F.P. and Delhi, under Section 66 (2) of the Indian Income Tax Act in the matter of the assessment of the Probynabad Stud Farm for the year 1930-31. [Ref. No. 12 of 1934].

The Commissioner's order of reference was as follows :—

"This is a petition on behalf of the Officer Commanding, Probyn's Horse, through his representative Messrs. Ferguson & Co., Chartered Accountants asking me to refer to the High Court of Judicature at Lahore, under Section 66 (2) of the Income Tax Act certain questions of law, arising out of the order passed under Section 31 by the Assistant Commissioner of Income Tax, in the matter of the assessment of the Probynabad Stud Farm, for the year 1930-31, *viz.*,

(1) Whether the Probynabad Stud Farm is an assessee under the Income Tax Act?

(2) If so, is its income not exempt from taxation within the meaning of Section 4 (3) (*i*)?

(3) Whether the income from *Dharat* (weighing charges) is not agricultural income as defined by Section 2 (1) (*b*) (*ii*) of the Act, and

(4) Whether the expenses claimed against *Dharat* income are not a permissible deduction under the Act ?

2. After hearing L. Kirpa Ram Bajaj, counsel for the petitioner, it has been agreed that the first two of the questions to be referred to the High Court should be formulated thus:—

(1) Whether in the circumstances of this case, the Officer Commanding Probyn's Horse, can be said to be an assessee under the Income Tax Act ?

(2) If the answer to the first question is in the affirmative is the income of the Probynabad Stud Farm not exempt from taxation within the meaning of Section 4 (3) (*i*) of the Act ?

The next two questions will stand as framed above.

2. FACTS OF THE CASE.—In order to make the position clear, it is necessary to give a resume of the origin, aims and objects of the Probynabad Stud Farm as supplied by the petitioner. The Probynabad Stud Farm was founded by Col. Probyn, the Officer Commanding the regiment known as Probyn's Horse in the year 1864. It appears that he obtained from Government a grant of certain lands in the Montgomery District and with the help of the funds collected from the sale of loote in China and with savings from certain subscriptions founded this farm, which was called after his name 'Probynabad Stud Farm'. It is stated that the pay of the regiment for one month was drawn twice through some mistake and this money was also invested in the farm. Occasionally there was a demand for funds from the regiment when pecuniary assistance became necessary. The management of the farm remains in the hands of the Officer Commanding, Probyn's Horse, for the time being, who works as an honorary trustee. The income derived from agriculture, securities, and other sources is utilised to finance the breeding of horses. The main object of the institution is to provide remounts for the regiment and the improvement of horse breeding in India. The majority of the horses thus bred are supplied to the Army Department on payment and stallions and brood mares are also imported: any stock found unsuitable as remounts are sold publicly.

The instrument of lease executed between Government and the Officer Commanding, Probyns Horse, does not define the purpose for which the lease of some 10,397 acres of land was granted, but the lessee has to pay the yearly rent by way of land revenue and malikhana and all rates and cesses.

As regards questions (3) & (4) the facts briefly are :—

It appears that the farm covers certain villages, the residents of which cultivate lands as tenants to the assessee and that the assessee also raises agricultural produce by cultivation It is a custom among cultivators, especially where the produce is to be accounted for between the landlord and the tenants, that the agricultural produce is got weighed or measured through a separate agency, called Dharwais, who are paid at certain stipulated rates for the job. Instead of allowing each tenant to engage his own Dharwai independently of the assessee, the latter appointed his own Dharwais for the entire farm by selling out the monopoly or right of weighing by public auction. The sale money is payable by certain monthly instalments and the auction purchaser obtains the exclusive right to weigh the produce in the village. The total realisations from such auctions amounted to Rs. 23,300 during the accounting period under consideration. In return for the auction purchase price, the Dharwais are allowed to charge the following rates:

(*a*) 2 per cent. on sales of all kinds of grain made in the godown of the farm.

(*b*) 1 per cent, on all kinds of grain purchased by the customers.

(*c*) 1 per cent. on all kinds of grain sold by the cultivator.

(*d*) 11 chattaks per maund for weighing the cotton and the grain at the *Kharif* crops.

(*e*) 8 seers per heap *Dheri* if it exceeds 10 maunds and 4 seers if it weighed less than 5 maunds.

4. The Income Tax Officer issued a notice under Section 22 (2) read with Section 34, calling upon the Manager of the Probynabad Stud Farm to file a return of its total income from all sources, assessable to income tax in the year 1930-31. In response to this notice a return was filed declaring an income of Rs. 32, under the head business and it was contended before the Income Tax Officer that the farm was not liable to be assessed to income tax. The Income Tax Officer framed three issues for decision namely,

(1) Whether there is any assessee under the Act?

(2) Whether in a case like this the property is held under trust or other legal obligation for advancement of an object of general public utility, entitling the farm to the exemption contemplated by Section 4 (3) (*i*) of the Act and

(3) Whther income from *Dharat* paid by Dharwais to the assessee was rent or revenue within the meaning of the expression as used in Section 2 (1) (*b*) of the Act?

The first issue was determined by the Income Tax Officer by holding that the assessee was an association of individuals. In regard to the second issue he found that the property was not held for the advancement of an object of general public utility, but that the entire benefits went to the members of this particular regiment. The third issue was decided by him as follows:—

"Income from *Dharat* cannot be regarded as exempt under Section 2 (1) (*b*) of the Act. It is not rent or revenue derived from land which is used for agricultural purposes. It arises from the transaction (weighing contracts) which are given to Dharwais. It is an incident of weighing and not of tenancy and therefore does not flow from the land. It does not even come within the purview of Section 2 (1) (*b*) of the Act, which defines agricultural income as under:—

"any income derived from such land by the performance by a cultivator or receiver of rent in kind of any process ordinarily employed by a cultivator or receiver of rent in kind to render the produce raised or received by him fit to be taken to market".

This sub-section contemplates the performance by a cultivator of a process ordinarily employed by a cultivator. Here there is no performance of any process by a cultivator but the performance of a process usually performed by a class of businessmen (Dharwais). Moreover, this process cannot be regarded as essential to render the produce fit to be taken to market".

With these remarks the Income Tax Officer held the income from *Dharat* to be chargeable to income tax. This income amounted to Rs. 23,300.

It appears that against this sum of Rs. 23,300 the assessee claimed a deduction of Rs. 5,793-6-3 by way of rebate paid by the assessee, out of which the Income Tax Officer allowed Rs. 2,799 as rebate and Rs. 1,300 for collection of *Dharat* and other charges, disallowing the rest on the ground that it was a sort of royalty

charged on contracts for weighing the Farm produce and that no expenses were incurred in earning this income from *Dharat*. He accordingly assessed the total income of the Farm to be Rs. 43,271 detailed as under :—

Interest on securities	Rs. 22,051
Dharat	,, 21,220
	,, 43,271

and levied a tax of Rs. 2,099-11.

9. An appeal was brought against the assessment on five grounds, four of which relevant to this reference were :—

(1) That the Probynabad Stud Farm was not liable to be assessed under the Income Tax Act.

(2) That the income derived from it did not come within the purview of any section of the Act, but on the contrary was exempt under Section 4 (3) (*i*).

(3) That in any event, the income from *Dharat* was exempt under Section 2 (1) (*b*) of the Income Tax Act, and

(4) That in the alternative, the entire expenses incurred in earning the income from *Dharat* should have been allowed.

In regard to the first objection, it was argued before the Assistant Commissioner that where there were no beneficiaries, as in this case, the provision of the Act did not apply and that the Officer Commanding Probyn's Horse, who was a trustee, could not be assessed to tax. In the course of his order, the Assistant Commissioner remarked : "It must again be admitted that there were decidedly no beneficiaries in this case, but trusts without beneficiaries are not unknown. The surplus funds of certain trust property or business may be applied for the improvement of the business itself. Examples of such trusts abound and the case of the farm is in itself an example in point. Chapter V of the Income Tax Act, to which a reference has been made, dealt with the liabilities in certain special cases, *i.e.*, the cases of minors, lunatics or idiots or persons residing outside British India. If these persons had a guardian, trustee or an agent in receipt of income, profits or gains chargeable to income tax on their behalf the provisions of that chapter lay down that tax would be levied upon and recoverable from such guardian, trustee or agent, as the case may be, in like manner and to the same amount as it would be leviable upon and recoverable from any such beneficiaries, if of full age, sound mind or resident in British India, and in direct receipt of such income, profits or gains. The case of the farms is

however, not covered by the provisions of this chapter. The taxation of trustees, other than those referred to in Chapter V is regulated entirely by Section 3 (*Sundaram*, 3rd Edition, page 864 bottom). In this view of the case, I think the assessment was rightly made on the Commanding Officer as a trustee for the surplus income in his hands ".

As regards the claim for exemption under Section 4 (3) (*i*), *i.e.*, objection (2), the Assistant Commissioner remarked that the income and profits of the farm were not distributed to anyone in the form of dividends but were utilised for purposes set forth in para 2 above. He added that the terms on which the farm was founded did not give the slightest indication that it was originally started or was to be subsequently run, for charitable purposes. He further added that the funds of the farm were not utilised for general public utility but that the savings if any were invested in Government securities or otherwise. He accordingly held that as there existed not even the remote or the ultimate object to apply the funds for charitable purposes, the exemption contained in Section 4 (3) (i) did not apply.

Objections (3) and (4) were disposed of by the Assistant Commissioner as follows :—

3. The Income-Tax Officer has given good reasons for holding that the income from *Dharat* could not be regarded as agricultural income as defined in Section 2 (1) (*b*) of the Act. It was surely not rent or revenue derived from land which was used for agricultural purposes. On the other hand, it arose from the transactions of contracts for weighment which were given to certain dharwais or weighmen. I agree with him that it was an incident of weighing and not of tenancy and the income, therefore, did not flow from the land. He was also right in holding that the income did not come within the purview of Section 2 (*b*)(1) (*ii*) either. This sub-section contemplates the performance by a cultivator of a process ordinarily employed by him. The process involved here was one which was performed by a class of businessmen called the dharwais. It cannot, by any stretch of argument, be regarded as process essential to render the produce fit for the market. It appears from the documents produced that the contracts of the various villages covered by the farm are sold by public auction. The sale money is payable by certain monthly instalments and the auction purchaser obtains the rights to weigh the produce in the village and to receive payment at certain specified rates. The

income derived by the sale of these contracts was in the nature of a business venture and was decidedly liable to assessment.

4. As against this income, the assessee claimed certain expenses. Some of the agreements usually executed by the dharwais were obtained. A reference to these showed that after the contract was obtained the dharwai could carry on the work on the following conditions:

(*a*) Payment of 2 per cent. on sales of all kinds of grain made in the godown of the farm.

(*b*) 1 per cent on all kinds of grain sold by the cultivator.

(*c*) 1 per cent on all kinds of grain purchased by the customers.

(*d*) 11 chattaks per maund for weighing the cotton and the grain at the kharif crops.

(*e*) 8 seers per heap (Dheri) if it exceeded 10 maunds and 4 seers if it weighed less than 5 maunds.

There were certain other conditions but these are not relevant to our purposes. The only section, the help of which could be invoked by the assessee, was Section 10 (2) (ix). This sub-section provides that the profits and gains under the head business shall be computed after making allowance for any expenditure (not being in the nature of capital expenditure) incurred *solely* for the purpose of earning such profits or gains. The conditions of the contracts indicate that the assessee was to incur no expenses for earning the *Dharat* income. The Income Tax Officer has allowed certain items in each assessment by way of rebate on *Dharat*, but the word 'rebate' seems to be a misnomer. The auditors for the assessee were unable to show from the books that any sums were paid by way of rebates to the dharwais. It appears that the items of Rs. 2,799, Rs. 1,446 and Rs. 1,209 allowed in the assessments of 1930-31 of 1931-32 and 1932-33 respectively related perhaps to the items credited to the account of *Dharwins* regarding *chattaks* per maund charged by the latter for weighing the produce of cotton during the *Kharif* crop, and 2 for weighing all kinds of grain belonging to the farm. The actual figures according to the accounts were, however as follows:

	Rs.	A.	P.
1930-31	5,793	6	3
1931-32	5,194	3	1
1932-33	2,851	14	5

The deductions allowed by the Income Tax Officer were in my opinion not admissible. The expenses claimed were neither rebates on *Dharat* nor incidental to this branch of the assessee's business. Once the *Dharwai* got the contract for weighing he worked in his own way and made his own income. If he weighed the produce of the assessee, he received payment for it and if he worked for another person, he was remunerated either in cash or in kind. The question is not whether the payments made were admissible as business deductions. In the present case, it is altogether clear that the payments made were connected with the agricultural business of the assessee and not with the contract for the sale of *Dharat.* Suppose the *Dharwai* obtained the contract without any previous payment, would the charges made by him for weighing the produce of the assessee be deductible from the agricultural or the other heads of income which are liable to tax? The answer is obvious. The charge related to the agricultural income and could be confined to this source only. The items claimed by the assessee in this connection were much in excess of those detailed above, but there were no accounts with regard to those. Since, however, the deduction was not at all admissible, I need not go into further details."

Having held this, the Assistant Commissioner by a separate order, dated 7-10-33, added back the sum of Rs. 2,799, to the assessment and rejected the appeal on other grounds.

6. I have now been approached with an application under Section 66 (2) of the Act, referred to above in the first paragraph of this reference.

7. Opinion of the Commissioner.

Question 1. The contention of the assessee is that there are no beneficiaries but that the Officer Commanding, Probyns Horse, acts as a trustee of the funds of the farm and therefore he cannot be treated as an assessee. Against this we have the fact that the lease of the land granted by Government is in the name of the Officer Commanding, Probyns Horse; the securities amounting to the considerable sum of 4½ lakhs of rupees are held in his name and the interest is credited to him. Under Sec. 2 (2) of the Income Tax Act, the term "assessee" means a person by whom income tax is payable and under Sec. 13 it is payable in respect of all income, profits and gains of any individual or other association of individuals. Whether the Officer Commanding is treated as an

individual in his position of trustee or as an association of individuals is not very material. It is not the Probynabad Stud Farm that is the assessee in this case, but the Officer Commanding Probyns Horse, on the income of the estate in his capacity as lessee of the farm land, trustee or whatever else he may be called. As he is responsible for carrying out the terms of the lease and for investing and spending the money, as trustee, on behalf of the Regiment, the answer must be in the affirmative.

Question 2. It is argued before me that the property is held under an oral trust. In order to be exempt the income must be so held wholly for religious or charitable purposes and in case of property so held in part only for such purposes the income applied or finally set apart for application thereto. Charitable purposes include relief of the poor, education, medical relief and the advancement of any other object of general public utility. There is no doubt whatever that the income is neither wholly nor partly set apart either for religious or charitable purposes. To assist any particular persons of the Regiment occasionally or their dependents out of the funds, or to breed horses for supply primarily to a particular regiment cannot by any stretch of the language bring the case within the definition of charitable purposes. My opinion therefore is that the question should be answered in the negative.

Question 3. The assessee's point is that the realisation from the sale of monopoly rights to the *Dharwais* are agricultural income within the definition contained in Section 2 (*i*) (b) of the Act, and therefore exempt from income-tax under Section 4 (3) (viii). This point has been dealt with by the Assistant Commissioner and I agree with his conclusion. Question 3 should accordingly be answered against the assessee.

Question 4. The assessee's claim is that the money which is paid to the weighmen by way of percentage on the sales of all kinds of grain made in the godown of the farm, etc., amounting to Rs, 5,793-6-3, should be deducted from the sum of Rs. 23,300. The question for consideration here is whether the wages which the farm, i.e., the assessee paid for getting his own agricultural produce weighed through the *dharwais* are a charge against the agricultural income of the assessee which has not been taxed, or a charge against the business income which has been taxed. It seems to me fairly clear that in so far as weighing charges paid by the assessee relate to the agricultural produce, the assessee is in the same position as an ordinary cultivator who will take into account

such charges as expenses for cultivation. The question should, in my opinion be therefore answered in the negative."

The case was heard by JAI LAL and SKEMP, JJ., and their Lordships delivered the following judgments and called for the supplementary statement from the Commissioner of Income-Tax:—

SKEMP, J.—This is a reference under Section 66 (2) of the Income Tax Act (XI of 1922) by the Commissioner of Income Tax at the request of the Officer Commanding Probyn's Horse, who has been assessed to income-tax in respect of the Probynabad Stud Farm.

The facts as stated by the Commissioner are that the Stud Farm was founded by Colonel Probyn, after whom the regiment takes it name, in the year 1864, by obtaining from Government a grant of certain lands in Montgomery District and with the help of funds collected from sale of loot in China, with a month's pay of the regiment said to have been drawn twice over and savings from certain subscriptions. The income from the Farm and other sources is used to finance the breeding of horses and the control of the Farm is in the hands of the Officer Commanding for the time being as trustee. The main object of the Stud Farm was originally to supply remounts for the regiment; since the Silladar System has been abolished it is used to provide remounts generally. The Commissioner states the majority of the horses bred are supplied to the Army Department on payment and stallions and brood mares are also imported. Any stock found unsuitable for remounts is sold publicly.

The Commissioner framed the following questions:

(1) Whether in the circumstance of the case the Officer Commanding Probyn's Horse, can be said to be an assessee under the Income Tax Act.

(2) If the answer to the first question is in the affirmative, is the income of the Probynabad Stud Farm not exempt from taxation within the meaning of Section 4 (3) (i)?

(3) Whether the income from *dharat* (weighing charges) is not agricultural income as defined by Section 2 (1) (b) (ii) of the Act: and

(4) Whether the expenses claimed against *dharat* income are not permissible deductions under the Act?

Question:—(*1*) A similar question in the *Tribune case* has been answered in the affirmative by JAI LAL, J., myself concurring,

and it is not necessary therefore to discuss this question at any length. In this case there is no difficulty in regarding the Officer Commanding Probyn's Horse, as an assessee. As has been laid down in *Hotz Trust* v. *Commissioner of Income Tax*, Section 40 of the Income Tax Act is merely a machinery section, and not a charging section and the person charged with tax is neither the trustee nor the beneficiary, as such, but the person in actual receipt and control of the income which it is sought to reach. In this case the person in receipt and control of the income is undoubtedly the Officer Commanding Probyn's Horse. This question must be answered in the affirmative.

Question (2).—Section 4 (3) of the Indian Income Tax Act runs :—

"This Act shall not apply to the following classes of income:—

(1) Any income derived from property held under trust or other legal obligation wholly for religious or charitable purposes and in the case of property so held in part only for such purposes the income applied, or finally set apart for application, thereto....."

In this sub-section " charitable purposes " includes relief of the poor, education, medical relief and the advancement of any other object of general public utility."

As to the meaning of the word 'charitable' here, the word "charity" has a technical meaning in English law derived from the preamble to the Statute 43 Elizabeth, Chap. IV. That statute was intended to provide for the reformation of abuses in the application of property devoted to charitable uses, yet, it contained in the preamble a list of charities so varied and comprehensive that it became the practice of the Courts to refer to it as sort of index or chart. (*Tudor on Charities*, Vth Edition, page 6). The Courts have subsequently extended it by analogous ideas.

One of the objects in the preamble to the Statute of Elizabeth was setting out of soldiers; consequently the English Courts have held that almost any object for the benefit of soldiers is a charity. For example, bequests to a volunteer corps, territorials, militia or yeomanry for their general purposes, a prize for some unspecified object to be competed for among cadets, or to an officers' mess for a library and a fund out of which to renew the books, or to a regiment for promoting sport for the benefit of its members, a gift to the National Rifle Association to be expended in teaching shooting, have all been held to be charitable (*Tudor, idem* page 40).

I am inclined to think that English cases are not to be relied upon in construing this section because in explaining "charitable purposes" the Legislature by using the words "for advancement of any other object of general public utility" has given a somewhat different conception of charitable purposes from that of the English Court. This conception is generally speaking wider but sometimes it is narrower and in dealing with soldiers it would be narrower. In my opinion the proper way to construe the section is to take the ordinary or dictionary meaning of charitable purposes, bearing in mind the explanation.

I think there is no doubt that the provision of remounts for the army is an object of general public utility. But most business is of public utility, and business on a large scale is often of general public utility, a fact particularly clear in the case of the great transport companies. But the fact that business is of general public utility does not exempt its profits from income tax. In the *Hotz Trust case* it might have been reasonably contended that the business, which owns several hotels in various places in Northern India, is of general public utility, but it was never suggested that the income was exempt on this account. I think therefore that the test whether the profits of a business carried on under a trust are exempt under the section is not whether the business is of general public utility but whether its profits go to charitable purposes including any object of general public utility.

Having got so far, I cannot find in the order of reference any clear statement as to what is done with the profits. There is apparently no deed of trust but the Officer Commanding for the time being administers the estate as a trust.

The Commissioners' order of reference contains the following:—

"Occasionally there was a demand for funds from the regiment when pecuniary assistance became necessary. The mangement of the farm remains in the hands of the Officer Commanding, Probyns Horse, for the time being, who works as an honorary trustee. The income derived from agriculture, securities and other sources is utilized to finance the breeding of horses. The main object of the institution is to provide remounts for the regiment and the improvement of horse-breeding in India. The majority of the horses thus bred are supplied to the army department on payment and stallions and brood mares are also imported, any stock found unsuitable as remounts are sold publicly."

The Commissioner further quoted the Income Tax Officer as finding "that the property was not held for the advancement of an object of general public utility but that the entire benefits went to the members of this particular regiment.

The Commissioner quoted the Assistant Commissioner as remarking "that the income and profits of the farm were not distributed to anyone in the form of dividends but were utilized for purposes set forth in para 2 above."

In para 2 above I cannot find any clear statement as to how the profits of this business are used. The Assistant Commissioner had said that "the surplus funds of certain trust property or business may be applied for the improvement of the business itself. Examples of such trusts abound and the case of the farm is in itself an example in point."

The Assistant Commissioner went on "that the terms on which the farm was founded did not give the slightest indication that it was originally started or was to be subsequently run, for charitable purposes". He added "that the funds of the farm were not utilized for general public utility but that the savings if any, were invested in Government securities or otherwise."

The Commissioner himself in dealing with the first question spoke of the Officer Commanding as responsible for carrying out the terms of the lease and for investing and spending the money as trustee on behalf of the regiment. In question No. 2 he said that there was "no doubt whatever that the income is neither wholly nor partly set apart either for religious or charitable purposes. To assist particular persons of the regiment occasionally or their dependents out of the funds, or to breed horses for supply primarily to a particular regiment cannot by any stretch of the language bring the case within the definition of charitable purposes."

This is all I have found as to the use of the profits and I would therefore return the case to the Commissioner for a re-statement as to the use to which the profits of the business are put.

JAI LAL, J.—I concur in returning the case to the Commissioner for a re-statement as indicated by my learned brother.

The Commissioner accordingly made a supplementary statement showing the nature of disbursements made during the preceding ten years. These showed, *inter alia*, that a sum of Rs. 1,74,518 was paid in the year 1924 as bonus to the regiment. Similarly in the years 1929 and 1930 sums to the extent of Rs. 6,000 odd and Rs. 3,500

odd were shown as unparticularised and in 1931, Rs. 23,118 was spent on farewell to the Commander-in-Chief. In 1926, Rs. 2,944 was spent for a Mess car and in 1931, Rs. 698 was spent on a wedding party.

The case then came on for hearing before SIR JAMES ADDISON, ACTING CHIEF JUSTICE, and MR. JUSTICE DIN MOHAMMAD.

M. C. Mahajan and *Kirpa Ram Bajaj* for the assessee.

J. N. Aggarwal and *Sarv Mitar Sikri* appeared for the Commissioner.

Their Lordships delivered the following judgment:

This is a reference under Section 66 (2) of the Indian Income Tax Act. The questions referred are as follows:—

1. Whether the Probynabad Stud Farm is an assessee under the Income Tax Act?

2. If so, is its income not exempt from taxation within the meaning of Section 4 (3) (i)?

3. Whether the expenses from *dharat* (weighing charges) is not agricultural income as defined by Section 2 (*b*) (*ii*) of the Act.

4. Whether the expenses claimed against *dharat* income are not a permissible deduction under the Act?

The reference originally came on for hearing before a Division Bench of this Court composed of JAI LAL and SKEMP, JJ. The learned Judges answered question No. 1 in the affirmative and without discussing questions Nos. 3 and 4 remanded the case to the Commissioner for a further statement on the use to which the profits received from the Probynabad Stud Farm were put, so as to be able to pronounce definitely on question No. 2. The supplementary statement having been received, we have now to decide questions Nos. 2, 3 and 4.

We may take up questions Nos. 3 and 4 first, as they proceed on a very simple ground. "*Dharat*" means weighing charges which in the case are levied by the assessee from the tenants of the land in addition to the rent which he receives from them. It is admitted that they form part of an agreement entered into with the tenants in that behalf. Section 2 (1) defines agricultural income which includes "the performance by a cultivator or receiver of rent-in-kind of any process ordinarily employed by a cultivator or receiver of rent-in-kind to render the produce raised or received

by him fit to be taken to market". In our view *dharat* income clearly falls within the provision of this sub-clause, and is, therefore, exempt from the provisions of the Income Tax Act. In this view of the case, question No. 4 does not arise.

The main controversy in this case has raged round question No. 2. It is contended on behalf of the assessee that the income received from the Probynabad Stud Farm is covered by Section 4 (3) (i) which exempts "any income derived from property held under trust or other legal obligation wholly for religious or charitable purposes, and in the case of property so held in part only for such purposes, the income applied, or finally set apart for application thereto." On behalf of the Commissioner, however, it is urged that the Farm is not a trust, much less a charitable trust, and, therefore, its income is not exempt from the operation of the Income Tax Act.

It may be remarked at once that there is no trust deed relating to this trust, nor does the instrument of lease executed between Government and the Officer Commanding Probyn's Horse define the purpose for which the lease of land was granted. All that is contended on behalf of the Stud Farm is that it is a trust by implication or what is known in law as an implied trust. The objects of this trust as stated by the Commissioner of Income Tax are as follows :—

"The income derived from agriculture, securities and other sources is utilised to finance the breeding of horses. The main object of the institution is to provide remounts for the regiment and the improvement of horse breeding in India. The majority of the horses thus bred are supplied to the Army Department on payment and stallions and brood mares are also imported. Any stock found unsuitable as remounts are sold publicly".

As stated above, the case was remanded to determine from the account books of the Farm, the nature of disbursements made by it during the last ten years, and the Commissioner has appended to his statement an annexure showing the details in respect thereof. This being the only material available before us and there being no deed in writing, we are compelled to form our opinion as regards the application of the income received from the Stud Farm from this document alone.

In support of his contention, counsel for the assessee has relied on *Tudor on Charities* (1929 edition page 40), *Pemsel* v. *Special Commissioners of Income Tax*, (1891 Appeal Cases 531 at

page 583); *Good In re, Harrington* v. *Watts* (1905, 2 Ch. D. 60); *Alt* v. *Stratheden and Campbell* (1894, 3 Ch. D. 265); *Moore* v. *Somerset, Donald In re*, (1909), 2 Ch. D. 410) and *Susanna D. Barker In re, Sherrington* v. *Dean of St. Paul's* (25 Times Law Reports 753 of the year 1909). It may be necessary, therefore, to examine these authorities to find out whether they are applicable to the facts of the present case or lay down any such proposition as is urged on behalf of the assessee.

Tudor on Charities at page 40 says as follows :—

"Although patriotic purposes are not necessarily charitable, a bequest to the Chancellor of the Exchequer to be appropriated by him to the benefit and advantage of Great Britain was a valid charitable gift.................The relief of taxation for setting out soldiers is one of the objects included in the preamble, and generally the maintenance of efficiency among soldiers is a charitable purpose. For example, bequest to a volunteer corps, territorials, militia or yeomanry for their general purposes, a prize for some unspecified object to be competed for among cadets, or to an officers' mess, for a library and fund out of which to renew the books, or to a regiment for promoting for the benefit of its members, are charitable. On similar grounds, a gift to the National Rifle Association to be expended in teaching shooting at moveable objects was held good."

It may be remarked in this connection that this particularly refers to what is known in English Law as the Statue of Elizabeth.

In *Pemsel* v. *Special Commissioners of Income Tax* (1891 A. C. at page 583), LORD MACNAGHTEN remarked as follows :—

"No doubt the popular meaning of the words 'charity' and 'charitable' does not coincide with their legal meaning and no doubt it is easy enough to collect from the books a few decisions which seem to push the doctrine of the Court to the extreme, and to present a contrast between the two meanings in an aspect almost ludicrous. But still it is difficult to fix the point of divergence and no one as yet has succeeded in defining the popular meaning of the word 'charity' * * * 'Charity' in its legal sense comprises four principal divisions: trusts for the relief of poverty, trusts for the advancement of education, trusts for the advancement of religion, and trusts for other purposes beneficial to the community not falling under any of the preceding heads."

In *Harrington* v. *Watts*; *Good In re*, a testator gave his residuary personality upon trust for the officers' mess of his regiment

to be invested and the income to be applied in maintaining a library for the officers' mess for ever, any surplus to be expended in the purchase of plate for the mess. It was held that a gift of residue to maintain a library and to purchase plate for the officers' mess being for a general public purpose tending to increase the efficiency of the army and aid taxation, was a good charitable bequest.

In *Alt* v. *Stratheden and Lord Campbell* it was held that a gift by will for the benefit of a volunteer corps was charitable bequest.

In *Moore* v. *Somerset, Donald In re* (1909, 2 Ch. D. 410) a testator devised and bequeathed the residue of his estate to trustees upon trust for sale and out of the proceeds to pay *inter alia* a legacy to the Officer Commanding the Northamptonshire Militia for the mess of that regiment or for the poor of the regiment. It was held that it was a good charitable gift and was payable to the Officer Commanding the unit of the Army Reserve which represented the Northamptonshire Militia.

In *Sherrington* v. *Dean of St. Paul's, Susanna D. Barker, In re* (25 Times Law Reports 753 of the year 1909), it was remarked that a gift to the Union Jack Club would have been a good charitable gift on the ground that the Club tended to improve the condition of soldiers.

In the first place, all these decisions have been pronounced under the English Statute, and secondly, they contemplate a regular trust which is enforceable at law and an express legacy enjoyed by the trust. Unfortunately, these conditions do not prevail here and, therefore, these decisions have no direct bearing on the question before us.

On behalf of the Commissioner, reliance has been placed among others on *Morice* v. *Durham* (32 English Reports 947), *Ex parte Rank's Trustees, R.* v. *Special Commissioners of Income Tax* (8 Tax Cases 286) and *Muhammad Ebrahim Malak* v. *Commissioner of Income Tax, Nagpur* (1930, 125 I. C. 879 (P. C.). In *Morice* v. *Durham* it has been held that a bequest in trust for such objects of benevolence and liberality as the trustee in his own discretion shall most approve, cannot be supported as a charitable legacy.

In *Ex parte Rank's Trustees, R.* v. *Special Commissioners of Income Tax*, it has been laid down that inasmuch as the settlor possessed under the deed of settlement power to execute an appointment in favour of purposes that were not charitable

the deed did not create a trust for charitable purposes only within the meaning of Section 105 of the Income Tax Act, (1842), and Section 37 (1) (*b*) of the Income Tax Act, (1918), although ultimately powers were exercised by the settlor in favour of charity.

In *Muhammad Ebrahim Malak* v. *Commissioner of Income Tax, Nagpur*, where the income of certain trust property vested in the head of a community and was applicable according to the terms of the deed of trust of carrying on the agricultural, industrial, commercial and other pursuits of the said community and for such donations for charitable or religious purposes, etc., as the then spiritual head and after him the spiritual head for the time being may deem fit, it was held by their Lordships of the Privy Council that the income from the trust property was not exempt from income tax under Section 4 (3) (i) of the Income Tax Act.

A glance at the annexure appended to the supplementary statement submitted by the Commissioner of Income Tax will clearly indicate that the decisions relied upon by the respondent are clearly applicable to the case before us. We find that in the year 1924 a huge sum of Rs. 1,74,518, was paid as bonus to the regiment. Similarly in the years 1929 and 1930 sums to the extent of Rs. 6,000 odd and Rs. 35,000 odd, respectively, are shown as unparticularised. In 1931, Rs. 23,113, appear to have been spent on "farewell to the Commander-in-Chief". In 1926 the Mess car account took away Rs. 2,944. In 1931, Rs. 698 had been spent on a wedding party. These disbursements will not justify the conclusion that the property is held in trust wholly for charitable purposes, nor can it be said to be so held in part as this question has been finally set at rest by the pronouncement of their Lordships of the Privy Council in *Muhammad Ebrahim Malak*'s *case*. The following passage from the judgment of their Lordships may be quoted with advantage :—

"Nor is it suggested that any part of the property is set aside for any charitable or religious purposes, so that it can be identified as appropriated exclusively to such purposes".

It is conceded by the assessee that no such setting apart or specification of the property has taken place in this case and in these circumstances it will not be possible to hold that even the second part of clause (*i*) of sub-Section (3) of Section 4 would apply.

Further, it is admitted that the element of discretion of the Officer Commanding who operates on the Stud Farm Fund

in making these disbursement as he thinks fit, is not altogether excluded. This will bring the Farm within the mischief of the rule enunciated by *Morice* v. *Durham*. However benevolent or liberal the objects of a trust may be, so long as the trustee has any discretion left in the matter, the trust cannot be supported as a charitable legacy. We are alive to the fact that most of the objects of the Stud Farm are no doubt charitable even within the technical sense of the term but we are regretfully constrained to remark that so long as the trust is not given a legal shape, by eliminating the element of discretion vesting in the Officer Commanding, it will not be able to claim the benefit of the exemption provided for in the Income Tax Act.

Counsel for the assessee had relied on *Sri Thakurji Maharaj* v. *Sukhdeo Singh* and has argued that mere breaches of trust by the trustee will not vitiate the trust and the object of the trust will remain the same as intended by its founder. Be that as it may, this principle of law does not help him nor does the decision relied upon by him lay down any such proposition of law which may be of any practical use to him in this case. The trust here fails as a charitable trust for want of certainty as to its objects and that defect cannot be cured so long as the Officer Commanding insists on his discretion in the matter. The object being laudable we consider that it will be quite in the fitness of things if with a view not only to secure an exemption under the provisions of the Income Tax Act but also to bring it on a legal footing, the Officer Commanding will give his considered thought to the matter and look into the desirability of reducing the terms of the trust to writing, so as to make them as definite and certain as the law requires.

For the reasons given above, we will answer question No. 2 in the negative. In view of the peculiar circumstances of the case, we will make no order as to costs.

Reference answered accordingly.

[IN THE LAHORE HIGH COURT.]

HITKARI BROTHERS
v.
COMMISSIONER OF INCOME TAX, LAHORE.

SIR JAMES ADDISON & ABDUR RASHID, JJ.

February 13, 1936.

FIRM—CONVERSION OF FIRM INTO COMPANY—ASSESSMENT OF COMPANY ON PROFITS OF FIRM AS ITS SUCCESSOR—RATE OF TAX APPLICABLE, WHETHER THAT OF COMPANY OR FIRM.

A firm was converted into a limited company on March 24, 1934 and the company took over the business of the firm as a going concern on April 1, 1934. The company was assessed in respect of the year 1933-1934 as the successor of the firm under Section 26 (2) of the Indian Income Tax Act and income tax was levied on the said income at the rate applicable to a company. The company contended that they should not be assessed on the profits of the firm at the rate applicable to a company :

Held, *on a reference by the Commissioner, that though the company was liable to pay tax as if it had received the whole of the profits of the previous year when its status was that of a firm, the assessment being on a company, the rate applicable to a company must be applied.*

COMMISSIONER OF INCOME TAX, BOMBAY *v.* WESTERN INDIA TURF CLUB, LTD. [1928] (I. L. R. 52 Bom. 123; A. I. R. 1928 P. C. 1; 106 I. C. 642; 55 I. A. 14; 54 M. L. J. 1; 2 I. T. C. 227) followed.

Case stated under Section 66 (2) of the Indian Income Tax Act by the Commissioner of Income Tax, Punjab, N.W.F. & Delhi Provinces (Ref. No. 60 of 1935).

Nawal Kishore, for the assessees.
Jagan Nath Aggarwal, for the Commissioner.

ORDER.

This reference by the Commissioner of Income Tax, Punjab, is concerned with the 1934-35 assessment of Hitkari Brothers of Jhelum. The Commissioner has stated that the assessees did not specify the contentions of law which should be referred and he himself summarised them in two questions. He then proceeded to refer the first question and to hold that no

question of law arose in the second and therefore he did not refer to this Court. The question referred is as follows :—

'Was the Income Tax Officer justified in assessing the petitioners at the rates applicable to a company and at the same time computing the income as that of a firm ?' Since the time this firm was first assessed, the status of the assessees had been that of a firm with three partners in equal shares. On the 24th March, 1934, the firm was converted into a company and was registered under the Companies Act, the subscribed capital being Rs. 45,000. There was no substantial change resulting therefrom as no outside shareholder was admitted. Shares were allotted to the partners equally. The company thus formed took over the business of the firm as a going concern on the 1st April, 1934. For the year 1933-34, which is the relevant account year for the assessment in dispute (1934-35), the status of the assessees was of a firm but it was changed into that of a company on the first day of the assessment year 1934-35.

What the assessees are objecting to is that they are being made to pay the tax on the income of the firm at the rate applicable to a company. The point they took was that if the profits were to be computed as if no change had occurred they should be allowed to derive the other benefits of being a firm, such as registration. As pointed out by the Commissioner, however, the case falls within the ambit of Section 26 (2) which runs as follows :

" Where, at the time of making an assessment under Section 23, it is found that the person carrying on any business, profession or vocation has been succeeded in such capacity by another person, the assessment shall be made on such person succeeding as if he had been carrying on the business, profession or vocation throughout the previous year, and as if he had received the whole of the profits for that year."

This section obviously means that the company which succeeded the firm is liable to pay tax as if it had received the whole of the profits for the previous year when the status was that of a firm. The assessment, however, being on a company, it would be the rate applicable to the company that must apply. This was so held by their Lordships of the Privy Council in *Commissioner of Income Tax, Bombay* v. *Western India Turf Club, Limited.* We, therefore, answer the question referred in the affirmative and direct that the assessees pay the costs of the Commissioner of Income Tax.

Reference answered.

[IN THE LAHORE HIGH COURT.]

H. T. CONVILLE

v.

COMMISSIONER OF INCOME TAX, LAHORE.

SIR JAMES ADDISON & ABDUL RASHID, JJ.

February 6, 1936.

AGRICULTURAL INCOME—INTEREST ON CAPITAL BORROWED FOR PAYING LAND REVENUE ETC., WHETHER ALLOWABLE—RENT OF SITE OF FLOUR MILL, LAMBARDARI FEES, COMMISSION RECEIVED FOR SELLING TENANTS' PRODUCE, WHETHER AGRICULTURAL INCOME—INDIAN INCOME TAX ACT (XI OF 1922), SECTIONS 2 (1), 4 (3) (vi), and 10 (2) (iii).

Section 10 of the Indian Income Tax Act applies to "Business" assessable under the Act and the allowances referred to in sub-section (2) of that Section cannot apply to agricultural income. Interest paid on money borrowed for the purpose of paying land revenue etc., cannot therefore be deducted under the provisions of Section 10 (2) (iii), in computing the income of an assessee.

Rent of the site of a flour mill cannot be regarded as rent or revenue derived from land used for agricultural purposes; it does not fall within any of the clauses of Section 2 (1) and cannot therefore be regarded as agricultural income.

Lambardari fees are not agricultural income and do not constitute any special allowance, benefit or perquisite specifically granted to meet expenses wholly and necessarily incurred in the performance of the duties of an office or employment of profit within the meaning of Section 4 (3) (vi) of the Income Tax Act and are not therefore exempt from income-tax.

Income derived from commission received by a landlord from the tenants for selling their produce on their behalf is not agricultural income and is not exempt from tax.

Case stated by the Commissioner of Income Tax, Punjab N.W.F. & Delhi Provinces. (Reference No. 55 of 1935).

Radha Kishen, for the assessees.

Jagan Nath Aggarwal, for the Commissioner.

ORDER.

This is a reference under Section 66 (2) of the Indian Income Tax Act.

The assessees are an unregistered partnership known as "Lessees of the Convillepur Farm", consisting of Mr. H. T.

Conville and his son Major L.H.G. Conville. The questions of law formulated by the Commissioner of Income-tax are as follows:

(1) When money is borrowed, which would probably not have been borrowed had not the assessee's own capital been invested in an income-producing business, is the interest paid on such borrowing deductible under Section 10 (2) (iii) from the income of that business?

(2) Is rent of a mill-site within the definition of agricultural income, Section 2 (1)?

(3) Are Lambardari fees within the definition of agricultural income, Section 2 (1)?

(4) Is the net profit from commission charged to tenants for sale of their produce on their behalf, within the definition of agricultural income, Section 2 (1)?

It appears that the assessees lend money to their tenants and during the accounting period they received Rs. 4,253 on account of interest on these loans. During the same period they paid interest amounting to Rs. 1,556 to their bankers. The case of the assessees is that they borrowed money from their bankers in order to pay the land revenue and to meet other agricultural expenses, and that they would not have been obliged to borrow this money had they not made loans to their tenants. On these grounds they seek to deduct Rs. 1,556 on account of interest paid to the bankers from the sum of Rs. 4,253 which they received on account of interest from their tenants. There is nothing on the record to show that Rs. 1,556 were paid by the assessees as interest on loans raised for the purpose of making the advances to their tenants which yielded the assessed income of Rs. 4,253 on account of interest. The learned counsel for the assessees submitted that the assessees were carrying on business as "Lessees of Convillepur Farm" and that Rs. 1,556 was the amount of interest paid by them in respect of capital borrowed for the purpose of the business, and that this sum was, therefore, exempt from the payment of income-tax under Section 10 (2) (iii) of the Income-tax Act.

Section 4, which is the main charging Section in the Act, provides that the Act shall apply to all income, profits or gains, as described or comprised in Section 6, from whatever source derived, accruing or arising, or received in British India. Sub-Section (3) of Section 4 enumerates the classes of income to which the Income Tax Act shall not apply. Agricultural income is one of

these classes of income. It is obvious, therefore, that agricultural income is totally excluded from the operation of the Income Tax Act and that the sources of income enumerated in Section 6 cannot include agricultural income. Section 10, therefore, applies to "Business" assessable under the Act, and the "allowance" referred to in Sub-section (2) of Section 10 cannot apply to agricultural income, but only to interest paid in respect of capital borrowed for the purposes of the "business" assessable under Section 6 of the Act. We are, therefore, of the opinion that the money borrowed by the assessees for the purposes of paying land revenue, etc., cannot be exempted from income-tax under the provisions of Section 10 (2) (iii).

Agricultural income is defined in Section 2 (1) of the Act. The rent of the site of a flour mill cannot be regarded as rent or revenue derived from land which is used for agricultural purposes. The working of a flour mill is not an agricultural purpose. The rent of the site of the flour mill does not fall within any of the other provisions of Section 2 (1) of the Act, and we are, therefore, of the opinion that it cannot be regarded as agricultural income.

It is contended by the learned counsel for the assessees that the income received from Lambardari fees comes within the exemption specified in Section 4 (3) (vi) of the Act, which runs in the following terms—

"Any special allowance, benefit or perquisite specifically granted to meet expenses wholly and necessarily incurred in the performance of the duties of an office or employment of profit".

A Lambardar is given remuneration for collecting land revenue at the rate of Rs. 5 for every 100 rupees of land revenue collected by him. If he carries on the collection personally he may not incur any expenses at all. If he employs some other person for the collection or if he has got to travel considerable distances he may incur some expenses. In the present case Lambardari fees amounted to Rs. 688. The Income Tax Officer has allowed an expenditure of Rs. 350 and has included the sum of Rs. 338 only as income from Lambardari fees. It is clear that the Lambardari fees do not constitute a special allowance, benefit or perquisite specifically grant to meet expenses *wholly* and necessarily incurred in the collection of the revenue. Section 2 (1) of the Act applies to the case of a person who gets agricultural income from the use of the land by direct operation. It is not applicable to a

person who gets certain fees which constitute his remuneration for the work of the collection of the land revenue.

The learned counsel for the assessees contended that the assessees undertake to sell the produce of the tenants either to Government or in the market, and that the commission which is charged really represents the expenses incurred by the assessees for cleaning, storing and drying the produce of the tenants before it is marketed. The Income-tax Officer has held, however, that only Rs. 400 were incurred as expenses for cleaning, drying, etc., by the assessees and he has, therefore, allowed these expenses out of the income of Rs. 2,403 derived by the assessees from commission charged on the disposal of tenants' produce. The net profit from commission does not fall within the definition of agricultural income under Section 2 (1) of the Act.

For the reasons given above, we answer all the four questions referred by the Commissioner of Income Tax in the negative. Parties will bear their own costs in this Court.

Reference answered accordingly.

[In the Lahore High Court.]

COMMISSIONER OF INCOME TAX, LAHORE

v.

HUKAM CHAND-JAGADHAR MAL.

Sir James Addison and Abdul Rashid, JJ.

January 24, 1936.

Bad Debt—When Debt Becomes Bad—Finding That Debt Had Become Bad in a Particular Year—Necessity of Sufficient Evidence.

In 1921 the assessee advanced Rupees 45,000 on a mortgage. He obtained a decree on the mortgage in 1925, brought the mortgaged properties to sale and for the unrealised balance of Rs. 26,721 he obtained a personal decree against his debtor in 1928. The debtor appealed to the High Court and his appeal was dismissed in 1931. In the meantime the assessee had been trying to execute the personal decree. The assessee claimed the above amount as a bad debt in computing his income for the year 1932-1933. The Income Tax Officer refused to deduct the amount, holding that it had become a bad debt in 1929. On appeal the Assistant Commissioner held that the debt had not yet become bad. The Commissioner agreed with the Income Tax Officer and held that the debt had become bad in

1929. Held, *on a reference by Commissioner, that there was no evidence for the finding that the debt had become a bad debt in 1929. The assessee would have been guilty of a fraud if he had attempted to claim it as a bad debt earlier than the year 1932-33 and whether it became a bad debt in that year or later was a question of fact to be decided by the Income Tax authorities.*

Case stated by the Commissioner of Income Tax, Punjab and N.W.F.P., under Section 66 (3) of the Indian Income Tax Act.

The Order of the High Court calling upon the Commissioner to state the case is reported as *Hukum Chand Jagadhar Mal* v. *Commissioner of Income Tax, Punjab* in Volume III of the *Income Tax Reports* at page 211 *et seq*.

Jagannath Aggarwal, for the Commissioner.

Shamair Chand, for the Assessee.

ORDER.

On the 1st of April, 1935, a Division Bench of this Court required the Commissioner of Income Tax to state a case and refer the following question for decision, namely—

' Whether there was any relevant and admissible evidence to support the conclusion that the sum of Rs. 26,721 became a bad debt in 1929 ? '

The facts are stated in the order of the Bench and in the reference now made by the Commissioner.

On the 2nd December, 1921, the assessee obtained a mortgage deed in his favour from *Sheikh Siraj Din* for Rs. 45,000, advanced as a loan. A suit was instituted in 1924 for the usual mortgage decree which was made on the 19th December, 1925. The property was sold and a balance of Rs. 26,721 remained due. A personal decree for the balance was obtained by the assessee against his debtor in 1928 and there was an appeal by the debtor to this Court against that decision. That appeal was not dismissed till the 26th November, 1931. In the meantime the assessee had been trying to execute the personal decree he had obtained although the appeal against it was pending. In the assessment year 1933-34 he claimed the above amount as a bad debt, the accounting period being 1932-33. The Income Tax Officer refused to grant him this relief on the ground that it had become a bad debt in 1929. The assessee appealed to the Assistant Commissioner who held that the debt had not yet become bad, as there was still time to proceed with the execution of the personal decree. The assessee went up to the Commissioner who upheld the original order

of the Income Tax Officer that the debt and become bad in 1929. It is in these circumstances that the question arose.

On the record we have no hesitation in finding that there is no evidence of any kind that the debt became a bad debt in 1929. The appeal against the personal decree was still pending and was not dismissed till the end of 1931. The assessee would have been guilty of a fraud if he had attempted to claim it as a bad debt earlier than the accounting year 1932-33. Whether it became a bad debt in that year or later remains a question of fact to be decided by the income tax authorities. With these remarks we answer the question referred in the negative. The assessee will have his costs from the Commissioner of Income Tax.

Reference answered accordingly.

[IN THE LAHORE HIGH COURT.]

BANARSI DAS

v.

COMMISSIONER OF INCOME TAX, LAHORE.

SIR JAMES ADDISON & ABDUR RASHID, JJ.

January 27, 1936.

BEST JUDGMENT ASSESSMENT—PARTIAL DEFAULT IN PRODUCTION ON ACCOUNT BOOKS—CONSEQUENCES—POWER OF INCOME TAX OFFICER TO MAKE BEST JUDGMENT ASSESSMENT—INDIAN INCOME TAX ACT (XI OF 1922), SECTION 23 (4).

The language of Section 23 (1) of the Indian Income Tax Act makes it clear that if the assessee fails to comply with all the terms *of a notice issued under sub-section (4) of Section 22, or, having made a return, fails to comply with* all the terms *of the notice issued under sub-Section (2) of Section 23, the Income Tax Officer can make an assessment to the best of his judgment. A partial default in the production of account books, therefore involves the same consequences under Section 23 (4) of the Act as a total default.*

Their Lordships also held on the facts that there was sufficient material to support the finding of the Income Tax Officer that the assessee was not prevented by any sufficient cause from complying with the notices issued to him under Sections 22 and 23.

Application under Section 66 (3) of the Indian Income Tax Act for a mandamus requiring the Commissioner of Income Tax Punjab, N.W.F. and Delhi Provinces to state certain points of law

in the matter of the assessment of *Rai Bahadur* Lala Banarsidas for the year 1932-1933.

Jagannath Aggarwal, for the Commissioner.

Achru Ram and *Asa Ram Aggarwal*, for the petitioner.

ORDER.

This is an application under Section 66 (3) of the Indian Income Tax Act for a mandamus to compel the Commissioner of Income Tax, Punjab, to state the case of *Rai Bahadur* Banarsi Das, and refer the points of law arising therein to this Court. The following points of law have been formulated on behalf of the assessee :—

"(1) Whether an Income Tax Officer is competent to review the order of his predecessor in office adjourning the case till the decision of the criminal litigation and start proceedings at his will without submitting the case to the Commissioner of Income Tax for revision of his predecessor's order under Section 33 of the Income Tax.

(2) Whether attendance in a Criminal Court under orders of a Magistrate is a sufficient cause for non-appearance before the Income Tax Officer within the meaning of Section 27 of the Act.

(3) Whether in the circumstances of the case the petitioner had reasonable opportunity to comply with the terms of the notices under Section 23 (2) of the Act or whether he was prevented by sufficient cause from complying with them.

(4) Whether the consequences contemplated by Section 23 (4) would follow the non-compliance with the second notice under Section 22 (4) at least to the extent to which the Income Tax Officer was satisfied that it had been complied with, specially when the second notice does not specify the points on which the account books were required as contemplated by Section 23 (3) of the Act,

(5) Whether in the circumstances of the case, the petitioner should be asked to produce the account books of the Kuldip Oil Mills, Lahore, which were not in his possession at that time and income from which was not liable to be assessed in his hands in view of the provisions of Section 26 (2) of the Income-tax Act and whether its non-compliance would warrant an assessment under Section 23 (4) of the Act.

(6) Whether when default in respect of notices under Section 22 (4) is not properly explained but the default of the notices under Section 23 (2) is satisfactorily accounted for, it is not the

duty of the income tax authorties to cancel the 23 (4) assessment, re-issue the notice under Section 23 (2) and make the assessment afresh.

(4) Whether assessment made by an Income Tax Officer to the best of his judgment under Sectin 23 (4) includes penal assessment.

(8) Whether in the circumstances of the case when the petitioner had requested the Income Tax Officer for transfer of the case was not the latter bound to grant some time for moving the Commissioner of Income Tax for that purpose if he was not prepared to forward the request of the petitioner to his superiors himself ".

The Commissioner of Income Tax has refused to refer the questions alluded to above. He has, however, taken action under Section 66 (1) of the Act and has propounded the following question of law for the opinion of this Court :—

" Whether as a matter of law it was not possible for the Income Tax Officer to find as fact that the assessee had failed to establish 'sufficient cause' or 'not reasonable opportunity' within the meaning of Section 27 of the Act " ?

The material facts of the case may be briefly stated. *Rai-Bahadur Lala* Banarsi Das is a millowner of Ambala. He carries on his business with an admitted capital of half a crore of rupees and his principal sources of income are Flour Mills, Oil Mills, Ice Factory, Banking and House property. He had paid no income tax since 1925-26 and had accumulated 5½ lacs of depreciation to be set off against future income. He submitted a return for the assessment year 1932-33 declaring a gross income of Rs. 25,639 against which, however, Rs. 76,885 was claimed on account of depreciation. The Income Tax Officer issued a notice on the 8th March, 1933, under Section 22 (4) of the Act calling upon the assessee to produce complete accounts of his income from all sources during 1931-32. This notice was not served on the assessee, and another similar notice was, therefore, issued on the 21st of March. In response to this notice some books of account were produced, which were examined partially by the Accountant on the 23rd March. The case was then adjourned to the 24th March when a number of other books relating to business at Ambala were examined. Books relating to Kuldip Oil Mills, Lahore, were, however, not produced by the assessee. On the 24th of March an application was filed on behalf of the assessee praying for eight months' extension of time for production of accounts relating to

Kuldip Oil Mills. It was stated in this application that as civil and criminal litigation between the assessee and his wife *Mussammat* Prem Kaur and Sardar Kartar Singh, the ex-Manager of the Mills, was going on at Lahore, the assessee was unable to produce the accounts of the Kuldip Oil Mills as these books were in Court. An assurance was given that the books would be produced as soon as they were given to the assessee by the Court. The Income Tax Officer thereupon passed the following order :—

"I adjourn the case *sine die.* Books of Kuldip Oil Mills to be called after the decision of the criminal case ".

It appears that in the beginning of July 1933, the Income Tax Officer who had been dealing with the case so far, was transferred and his successor issued a notice under Section 22 (4) of the Act on the 10th of July for the production of assessee's accounts from all sources of income on the 22nd of July. The peon went with a notice to the assessee's place of business on the 11th of July. He was told that the assessee had gone to Lahore and his agents, Uggar Sen and Jagan Nath, who had been appearing in income-tax matters previously refused to accept service of the notice. The notice was, therefore, affixed to the door of the premises in the presence of the agents of the assessee. The assessee on the 21st of July wrote from Lahore making enquiries about this notice, and the Income Tax Officer sent a reply stating that as a special case he would give the assessee another opportunity to produce his accounts on the 1st of August, 1933. With this letter a notice under Section 23 (2) of the Act was also sent asking the assessee to produce any evidence on which he wished to rely in support of his return on the 1st of August, 1933. These notices were served on the assessee after the fixed date, *i. e.*, on the 2nd of August. The Income Tax Officer therefore, issued fresh notices on the 5th of August for production of accounts on the 15th of August. In reply to the first issue of notices a letter dated the 7th of August was received from the assessee to the following effect—

"It would appear from correspondence in your office that your predecessor had already granted me time till the 31st October, 1933. Thus there is no question of any adjournment in this connection ".

In reply to the second notice the assessee sent a letter dated the 13th of August stating that the Ambala accounts had already been examined, and that an extension of eight months had been allowed for the production of the Oil Mills accounts. It was

stated in this letter that the Income Tax Officer was helping those who were responsible for involving the assessee in baseless litigation at Lahore and that the income-tax machinery was being misused in order to assist the enemies of the assessee.

It is unnecessary to give details of further correspondence between the assessee and the Income-tax Officer. Suffice it to say that the Income-tax Officer in one of his letters stated that if any of the books on which the assessee relied were in "some Court or elsewhere", the assessee should give the requisite information and the Income-tax Officer will take proper steps to have them produced. In reply the assessee stated that the account books of the Kuldip Oil Mills were in the control of the Trustees of *Rai Bahadur Lala* Banarsi Das Trust at Lahore which was then functioning. As no books were produced on the 15th of August the Income-tax Officer gave a further opportunity to the assessee and issued fresh notices for the 2nd of September under Sections 22 (4) and 23 (2) of the Act. These notices were accompanied by a covering letter requesting the assessee to assist the Income-tax Department in arriving at a correct estimate of his income, and also pointing out the consequences of failure to comply with the notices. These notices were served on the 18th August, 1933. As no appearance was put in by or on behalf of the assessee on the 2nd September the Income-tax Officer proceeded to assess the income under Section 23 (4) of the Act to the best of his judgment and the assessment was completed on the 8th of September, 1933.

The first question of law formulated on behalf of the assessee was not pressed by the learned counsel during the course of his arguments. The second and the third questions fall within the ambit of the question of law referred by the Commissioner of Income Tax under Section 66 (1) of the Act. We, therefore, proceed to deal with question No. 4. The Commissioner of Income-tax found it difficult to understand this question. We also find that the language in which question No. 4 is framed is very involved. It was explained to us by the counsel that the real meaning of question 4 is, "whether, if there is only partial default in the production of account-books, can an assessment be made under Section 23 (4)". The language of Section 23 (4) makes it clear that if the assessee fails to comply with *all the terms* of a notice issued under sub-section (4) of Section 22 or, having made a return, fails to comply with *all the terms* of a notice issued under sub-Section (2) of Section 23, the Income Tax Officer shall make the

assessment to the best of his judgment. A partial default therefore involves the same consequences under Section 23 (4) of the Act as a total default.

With respect to question 5 it was contended by the learned counsel for the petitioner that as the Kuldip Oil Mills had been handed over to a Trust before August 1933, the assessment should have been made against the Trust which was the successor of the assessee with respect to the Oil Mills business under the provisions of Section 26 (2) of the Act. This point was never raised in the proceedings before the Income Tax Officer. Moreover it had not been established on the record that the trust had succeeded to the Oil Mills business before August 1933. The onus on the question of establishing the succession with respect to the business lay upon the assessee. He did not furnish any particulars of the Trust and did not even forward a copy of the Trust deed to the Income Tax Officer before the assessment was made. The fact of succession not having been established, the fifth question formulated by the assessee does not arise so far as the assessment of 1932-33, now under consideration, is concerned.

Question 6 practically involves the same point as question No. 4 and it is unnecessary to deal with it separately.

The point underlying question No. 7 is whether the assessment made by the Income Tax Officer was not to the best of his judgment but was a *mala fide* and perverse assessment. We are of the opinion that there is no evidence or indication on the present record which may show that the Income Tax Officer was acting in a *mala fide* manner. As pointed out by the Commissioner an assessment at 6½ lacs on a person with half a crore of capital could hardly be described as *mala fide*. We are further of the opinion that the Income Tax Officer acted in a perfectly *bona fide* and reasonable manner in allowing the assessee a large amount of depreciation in various accounts and in assessing his net income at the sum of Rs. 55,066. On the above finding of fact, question 7 does not arise. Question 8 was not pressed by the learned counsel for the assessee.

With reference to the question referred by the Commissioner under Section 66 (1), we are of the opinion that the letters of the assessee furnish sufficient material for the finding of fact that the assessee was deliberately delaying the assessment and that he was not prevented by any sufficient cause from complying with the notices issued to him under Sections 22 and 23 of the Act. There

is also material for the finding that the assessee had reasonable opportunity to comply with the different notices and it was, therefore, open to the Income Tax Officer to find as fact that in spite of reasonable opportunity the assessee had failed to comply with the notices issued to him under Sections 22 and 23.

For the reasons given above, we dismiss the petition for a mandamus. So far as the question referred by the Commissioner is concerned, we hold that "it was possible for the Income Tax Officer to find as fact that the assessee had failed to establish 'sufficient cause' or 'not reasonable opportunity' within the meaning of Section 27 of the Act". In view of all the circumstances, we leave the parties to bear their own costs in this Court.

Reference answered.

[IN THE CALCUTTA HIGH COURT.]

In the matter of BABULAL RAJ GARHIA.

SIR HAROLD DERBYSHIRE, C. J., and COSTELLO, J.

February 28, 1936.

PROPERTY—*Bona fide* ANNUAL VALUE—QUESTION OF FACT—LEASE DEED STIPULATING ANNUAL VALUE NOT CONCLUSIVE EVIDENCE—REFERENCE—QUESTIONS NOT RAISED BEFORE COMMISSIONER—QUESTION WHETHER THERE IS A SUCCESSION, WHETHER QUESTION OF LAW—INDIAN INCOME TAX ACT (XI OF 1922), SECTIONS 9 (1), 66 (2) AND (3).

A lease deed stipulating an annual rental value, though a piece of evidence, is not conclusive edidence of the bona fide *annual value of a property. The* bona fide *annual value is a question of fact and in determining that value all the circumstances of the case must be considered.*

The High Court has no power to require the Commissioner of Income Tax under Section 66 (3) of the Indian Income Tax Act to refer a question of law which was not raised by the assessee before the Commissioner in his application under Section 66 (2) of the Act.

Where the assessee who was the propietor of a jute mill sold the mill to a private limited company in which he held almost all the shares, without transferring the debts and outstandings of the mill : Held, *that the question whether or not there was a succession to the jute mill within the meaning of section 26 (2) of the Indian*

Income Tax Act was a question of fact and the Commissioner could not be required to refer this question to the High Court.

Application under Section 66 (3) of the Indian Income Tax Act to require the Commissioner of Income Tax, Bengal, to state a case in the matter of the assessment of Babulal Rajgarhia for the year 1933-1934.

On the application of the assessee the High Court issued a rule calling upon the Commissioner of Income Tax to show cause why he should not draw up a statement of the case on these questions of law. The Commissioner in showing cause why he should not be required to state the case submitted as follows :—

"As directed by their Lordships, the Hon'ble Judges of the Calcutta High Court in their order No. 2382, dated the 8th July, 1933, in the above matter, I have the honour to show cause why I should not draw up a statement of case on the questions referred to in the schedule attached to that order.

2. This matter arises out of an assessment made on Babulal Rajgharia as an individual for the year 1933-34 and on the income of the year of account Dewali 1988-89 (ending November 1932). For the relevant year the assessee in his return showed a loss of Rs. 73,573-6-10. The Income Tax Officer after having called for his account books under Sections 22 (4) and 23 (3) of the Income Tax Act and on an examination of the books produced computed his income as follows :—

Property	...	Rs. 84,702
Business loss	...	,, 45,164
Other sources	...	,, 7,516
	Total income	47,014

He found the assessee's sources of income to be (1) house properties, (2) business in mica, (3) running a jute mill under the name and style of Kedarnath Jute Manufacturing Company, (4) money-lending, (5) supply business with the Corporation.

As regards the house properties the assessee owns one at 5/1 Russel Street and 13 others at different places in Calcutta. The *bona fide* annual value for the premises at 5/1, Russel Street, has been computed by the Income Tax Officer at Rs. 45,002, and the assessee no longer disputes this valuation. The dispute is regarding the *bona fide* annual value for the remaining 13 properties. There is no dispute that for the first 9 months these properties

could be let out for Rs. 62,930. This is evidenced by the bills issued and realised by the assessee for that period of 9 months. On this evidence as also on the evidence of municipal valuation and of letting value of similar premises in their respective localities the Income Tax Officer making allowances for rates and taxes and vacancies computed the *bona fide* annual value at Rs. 45,964. Assessee's contention is that the valuation should be only Rs. 12,000 and for this purpose he wants to take his stand on a deed of lease dated the 25th August, 1932, by which the properties were leased by him at a rental of Rs. 1,000 per month to a private limited company styled Babulal and Company, Limited which was formed in 1932 and in which the assessee himself was allotted 100 shares while the balance of 5 shares was alloted to his nephew Jamuna Prosad. The lease was to run for 5 years but was liable to cancellation on six months notice given by either party and on the strength of this lease the assessee claimed that the *bona fide* annual value of the house property in question for the purpose of the computation of his taxable liability under Section 9 of the Act was Rs. 12,000 and that he should be taxed on the income from this property accordingly.

3. The assessee's appeal against this method of computation failed as also his application subsequently filed under Section 66 (2) of the Act and arising out of this matter. Their Lordships have asked me to show cause why I should not state a case to the Court on the questions which I set out below :—

'Whether a lease deed stipulating an annual rental of a house property is not conclusive evidence to prove *bona fide* annual value as stipulated by Section 9 (1) of the Income Tax Act '.

Under Section 9 of the Income Tax Act, tax is payable by an assessee under the head ' property ' in respect of the *bona fide* annual value of such property '*bona fide* annual value' means the sum for which the property can reasonably be expected to let from year to year (Section 9 (2) of the Act). The assessee's claim is that the lease deed referred to above is conclusive evidence in proof of the *bona fide* annual value as contemplated by that section. I would respectfully submit that this is wrong and the first contention I would respectfully urge is that the question 'what is the *bona fide* annual value' is a pure question of fact (cf. *Sir Hari Singh Gour* v. *Commissioner of Income Tax, Central Provinces*, 3. I.T.C. 323). I would also urge that while the sum at which house property may have been let in the year of account or for part of the year of

account is material evidence, it is not conclusive evidence of the annual value and that for the purpose of determining this sum all the circumstances of the case must be taken into consideration (*Soratee Bara Bazar Company Limited* v. *Commissioner of Income Tax, Burma* 5 I.T.C. 21). An English case, the facts of which are very similar to this, is *Stocks* v. *Sully* (4 T.C. 98) where a mother granted to her son a lease of a public house at a rent of £ 19 10s. and where the Court affirmed the determination of the Income Tax Commissioners that they were not bound to accept the lease in the circumstances as conclusive evidence of the annual value of the premises and fixed that value at £ 40. The circumstances here are that the assessee in his individual capacity gave a lease of this house property to a private limited company in which he held a controlling interest and at a rate of rent which was only about 1-16th of the rent which he was realising in former years and in the first nine months of the year of account before he transferred the property to the private company. My respectful opinion is (a) that the question at issue is altogether one of fact (b) that a lease deed stipulating an annual rental value though a piece of evidence, is not conclusive evidence of the bona fide annual value of the property and that in determining that value all the circumstances of the case must be considered.

4. The second question on which I am asked by their Lordships to show cause why a case should not be stated is as below :

'Whether or not there was a succession within the meaning of Section 26 (2) of the Act of the Jute Mill of the Assessee which was sold without transferring the account books, debts and outstandings etc.'

In this connection, the material facts are as follows. The assessee in his individual capacity was the proprietor of a jute mill named the Kedarnath Jute Manufacturing Company. This mill worked uptil the 9th October, 1932, and on the 12th October, 1932 the mill was sold to a private limited company styled the Kedarnath Jute Manufacturing Company Limited. This private company come into existence in May, 1932. The assessee held 25,396 shares out of the total shares of 25,500 ; 50 were held by his nephew Jamuna Prosad and the other 54 by outsiders. This new company was entitled to start business on the 17th October, 1932 but, actually began on the 29th October of that year. The assessee's contention before the income-tax authorities was that

there was no succession within the meaning of Section 26 of the Act and that therefore he was entitled in his individual capacity to set off from his profits arising from any other source loss incurred in the jute business in the year of account. The whole transaction is very anomalous. There was no deed of transfer and the property was transferred by a mere cash memo, part of the price being represented by the shares which the vendor took in the new company. This company took over the buildings, machinery, stock and stores on a valuation, while the land on which the mill stood was leased by the assessee to the new company on a monthly rent of Rs. 60 for 99 years.

5. Discontinuance was claimed on two grounds—one, because there was an interval. between the cessation of the old business and the starting of the business by the new company, secondly, because the new company did not take over any of the outstandings or accept responsibility for the liabilities of the predecessor. This, in my respectful view, does not constitute discontinuance. A business of the same character as before is being carried on in the same premises and to all intents and purposes so far as the constituents are concerned, under the same name and with practically the same staff. If the manager is changed or is there was an interval of a few days between the cessation of working by the predecessor and the commencement of the work by the successor, that makes no difference. The old business was not wound up or any new business started. The same business continued all through and all that happened was that there was a change in the ownership from an individual to a limited company. If debts and outstandings were not transferred to the new company, I do not think this really affects the issue and the reason why no such transfer was effected may have been that the liabilities of the old concern were approximately equal to the outstanding debts due to it, the former figure being 68,342 and the latter 62,539 while a further reason for the course adopted in this case may have been that although there was technically a succession, the successor was virtually its predecessor under another name.

6. The third question with regard to which I am asked to show cause why I should not state a case is as follows:

'whether assuming that there was a succession under Section 26 (2) of the Act the assignee (assessee) was entitled to deduction for the losses incurred by him in the business.'

The assessee never before raised this question in this form and my respectful submission would be that he cannot be allowed to raise this question at this stage when it was not raised in this form either before the Income Tax Officer, the Assistant Commissioner of Income tax or myself. (*Trustees Corporation* (*India*) *Limited* v. *Commissioner of Income Tax, Bombay*, Privy Council decision, 4 I.T.C. 378 and *Maharaj Kumar Ram Rambijaya Prasad Singh, Maharaja Bahadur of Dumraon* v. *Commissioner of Income Tax, Bihar and Orissa* 7 I.T.C. 483). Before me the assessee claimed set off of this loss against his profits, definitely on the ground that there was discontinuance. He did not put his case in the form now presented before their Lordships. He resolutely repelled any suggestion even as to there having been any succession in this case. So the question as now framed was never before the Income Tax authorities and as such I would respectfully urge that the assessee is now debarred from raising this question at this stage. Should their Lordships however not accept this view but hold that this question can now be raised, it would certainly be a question of law. But I would submit that as the answer to the question should be in the negative, I should not be asked to state a case on this question either. If there was a succession within the meaning of Section 26 (2), assessment in respect of this income must be made on the successor, that is, on the private company and not on this individual and the profit or loss resulting from the working of this business in the year of account must be taken into consideration in determining the successor's profits. It is true that under Section 24 (1) where any assessee sustains a loss of profits or gains in any year under the heads mentioned in Section 6, he should be entitled to have the amount of the loss set off against his income, profits or gains under any other head in that year. This section, however, has, in my respectful opinion no applicability in this case, because under Section 26 (2) of the Act he is not an assessee in respect of this business from which a loss accrued in the previous year and it would certainly be anomalous if the position were that in case of a succession under Section 26 the predecessor could claim to set off a loss against his other income, while the successor must be taxed in respect of the profits of the transferred business.

7. For the reasons stated above, it is respectfully urged that this rule should be discharged with costs ".

S. N. Banerji, for the assessee.

Dr. R. B. Pal, for the Commissioner of Income Tax.

DERBYSHIRE, C. J.—This Rule must be discharged with costs.

In the letter which the Income Tax Commissioner has sent to this Court under the rules of this Court showing cause against the Rule which we ordered to issue, the first question submitted is "Whether a lease deed stipulating an annual rental of a house property is not conclusive evidence to prove the *bona fide* annual value as stipulated by Section 9 (1) of the Income Tax Act". The Commissioner of Income Tax submits that the question is altogether one of fact and that a lease deed stipulating an annual rental value, though one piece of evidence is not conclusive evidence of the *bona fide* annual value of the property and that in determining that value of the property all the circumstances of the case must be considered. Mr. Banerji who appears in support of this Rule admits that that contention is right.

The second question submitted "is whether or not there was a succession within the meaning of Section 26 (2) of the Act to the Jute Mill of the assessees which was sold without transferring the account books, debts and outstandings etc." The Income Tax Commissioner has set out the facts relating to the transfer of building machinery, stocks and stores and the land on which he built. He submits this again as a question of fact. I think that it is a question of fact and Mr. Banerji does not argue to the contrary. So, that question goes.

The third question with regard to which the Commissioner of Income tax is asked to show cause why he should not state a case is as follows: "Whether assuming that there was a succession under Section 26 (2) of the Act the assessee was entitled to the deduction for the losses incurred by him in the business". The Commissioner of Income Tax says that that question was never raised before in this form and in his submission the assessee ought not to be allowed to raise it at this stage when it was not raised in this form either before the Income Tax Officer, the Assistant Commissioner of Income Tax or the Commissioner of Income Tax.

Now, this Rule was issued under the provisions of Section 66 of the Income Tax Act. Section 66 sub-Section (1) is as follows: "If in the course of any assessment under this Act or any proceeding in connection therewith other than a proceeding under Chapter VIII, a question of law arises, the Commissioner may, either on his own motion or on reference from any income tax authority subordinate to him, draw up a statement of the case and refer it with his own opinion thereon to the High Court." The Rule was not

issued under that section. The Rule was applied for under the next sub-section, sub-Section (2) of Section 66, which says "within sixty days of the date on which he is served with notice of an order under Section 31 or Section 32 or of an order under Section 33 enhancing an assessment or otherwise prejudicial to him or of a decision by a Board of Referees under Section 33-A the assessee in respect of whom the order or decision was passed may, by application accompanied by a fee of one hundred rupees or such lesser sum as may be prescribed, require the Commissioner to refer to the High Court any question of law arising out of such order or decision, and the Commissioner shall, within sixty days of the receipt of such application, draw up a statement of the case and refer with his own opinion thereon to the High Court. Provided that a reference shall lie from an order under Section 33 only on a question of law arising out of *that order itself and not on a question of law arising out of* a previous order under Section 31 or Section 32, revised by the order under Section 33. Provided further that if in exercise of his power of revision under Section 33, the Commissioner decides the question or if the Commissioner rejects the application on the ground that it is time barred or otherwise incompetent, or if, in exercise of his powers under sub-section (3), the Commissioner refuses to state the case, the assessee may within thirty days from the date on which he receives notice of the order passed by the Commissioner withdraw his application, and if he does so, the fee paid shall be refunded". Then sub-section (3) says "If on any application being made under sub-section (2) the Commissioner refuses to state the case on the ground that no question of law arises the assessee may apply within six months from the date on which he is served with notice of the refusal to the High Court, and the High Court, if it is not satisfied of the correctness of the Commissioner's decision, may require the Commissioner to state the case and to refer it, and, on receipt of any such requisition, the Commissioner shall state and refer the case accordingly". The rest of the sub-section is not relevant.

On the 22nd December, 1934, the assessee purported to make an application under Section 66 (2) of the Income-tax Act headed "For the assessment year 1933-34", saying "Your petitioner most humbly prays that the following points of law which arise out of the assessment proceedings to the assessee named above, may kindly be referred to the High Court of Judicature at Calcutta, under Section 66 (2) of the Indian Income tax Act, XI of 1922,

for determination with reference to the facts and circumstances of the case referred to above.

(1) Whether a lease deed stipulating an annual rental value of a house property is not a conclusive evidence to prove the *bona fide* annual value as contemplated by Section 9 (1) of the Income Tax Act ?

(2) Whether the Inceme Tax Officer was right in assessing to income tax the same income under Section 9 twice, *viz.*, once in the hands of the lessor and for the second time in the hands of the lessee ?

(3) Whether or not there was a succession within the meaning of Section 26 (2) of the Act to the Jute Mill of the assessee which was sold without transferring the account books, debts and outstandings, etc. ?

Your petitioner would be much pleased to withdraw the above application if the points of law were decided under Section 33 of the Act no prejudicial to the interests of assessee.

The question we are concerned with now, as I read out before is whether assuming that there was a succession under Section 25 (2) of the Act the assessee was entitled to deduction for the losses incurred by him in the business. It is quite clear when the application made by the assessee under Section 66 (2), which is the foundation of this proceeding, was made, that the question which is now sought to be raised was never mentioned at all. It is another matter due to an after-thought, which has been raised since. Under those circumstances it appears to us that the assessee is not, to use the words of the Act, entitled to require the Commissioner to refer to this Court this particular question of law. If he were in a position to do that he should have raised it in his application under Section 66 (2). That he did not do. Consequently we do not order that the Income Tax Commissioner should state a case on this particular question.

The result is that the Rule issued in this matter is discharged with costs. The total costs of the Income Tax Commissioner are assessed with the consent of the applicant at Rupees one hundred and fifty.

COSTELLO, J.—I agree.

Rule discharged.

[IN THE CALCUTTA HIGH COURT].

In the matter of GOPIRAM GOBINDRAM.

SIR HAROLD DERBYSHIRE, C. J., and COSTELLO, J.

February 28, 1936.

APPROPRIATION OF PAYMENTS—GENERAL RULE—MORTGAGE DEED—STIPULATION THAT PAYMENT SHOULD BE CREDITED IN THE FIRST INSTANCE TOWARDS INTEREST—APPROPRIATION TOWARDS PRINCIPAL—LEGALITY—REFERENCE—FORM OF QUESTIONS—COMBINED QUESTIONS, IMPROPRIETY OF—INDIAN INCOME TAX ACT (XI OF 1922), SECTION 66 (2).

Where interest is outstanding on a principal sum due and the creditor receives an open payment from the debtor without any appropriation of the payment as between capital and interest by either debtor or creditor, the presumption is that the payment is attributable in the first instance towards the outstanding interest.

Further, where there is a definite stipulation in a mortgage deed that moneys paid should be apporpriated in the first instance towards interest and the balance set off against the principal, income-tax authorities are entitled to assume that the mortgagee has applied the moneys received in accordance with the provisions of the mortgage deed, that is to say, that the mortgagee has appropriated the moneys in the first instance towards the interst.

DERBYSHIRE, C.J.—*When questions are referred for the opinion of the High Court two or more questions should not be combined and rolled up in the form of one question. Each question must be stated separately. Further, the questions should not be divorced from the facts of the particular case and should not be in the abstract.*

COMMISSIONER OF INCOME TAX, BENGAL *v.* SIR KAMESWAR SINGH [1933] (I. L. R. 12 Pat. 318; 1933 1 I. T. R. 49; 6 I.T.C. 401; A.I.R. 1933 P.C. 108) *applied.*

Case stated by the Commissioner of Income Tax, Bengal, under Section 66 (3) of the Indian Income tax Act in the matter of the assessment of Gopiram Gobindram for the year 1932-33. [Ref. No. 8 of 1934].

The facts appear from the following statement of the Commissioner.

STATEMENT OF CASE.

" As directed by Their Lordships, the Hon'ble Judges of the Calcutta High Court in their order dated the 9th January, 1935, and passed under Section 66 (3) of the Income Tax Act, a statement of

case is drawn up and submitted for Their Lordships' decision on the question of law formulated immediately below :—

"Whether it is open to a mortgagee notwithstanding the mortgage deed to apply payments, or in case when the mortgagee has taken possession, the net realisations of the mortgaged property, towards interest, to appropriate such payments or realisations with or without the consent of the mortgagor towards principal?"

2. **Facts of the Case.**—This matter arises out of assessment made for the year 1932-33 by the Income Tax Officer, District IV (2), on the assessee, a Hindu Undivided Family, and on the income of the year of account 1987-88, *Rathjatra* ending in June or July 1931. For that assessment the assessee submitted a return on 20th September, 1932 under Section 22 (2) of the Income Tax Act showing a loss of Rs. 44,297 and was assessed on 16th December, 1932 by the Income Tax Officer on a total income of Rs. 89,087 made up as follows :—

		Rs.
Interest on securities	...	510
Income from property	...	67,013
Income from business	...	13,304
Income from other sources	...	8,206
	Total	89,087

On appeal the Assistant Commissioner on 4th December, 1933 reduced the assessment by a sum of Rs. 12,000 (this being the amount which the Income Tax Officer had calculated and taxed as interest accrued on the outstandings of a constituent in the year of account on the ground that it was humanly certain that not only would no interest be realised from this constituent but in all probability the principal itself was endangered.

3. The material facts out of which this question now before Their Lordships has arisen are set out below. Raghunath Das Shewlal had in the year 1908 taken a lease for a period of 38 years of premises at 63, Clive Street, from one Nando Lal Mullick. These leaseholders are related by marriage to the assessee and when they found themselves in financial difficulties at a later date, they borrowed five lakhs of rupees in 1929 from the assessee and by a deed dated the 23rd July of that year, a copy of which is appended to this statement of case and marked A, they gave a mortgage of this leasehold property to the assessee. By a further and supplementary deed dated the 14th January, 1930, a copy of which is

marked B and appended to the statement of case, a further loan of one lakh of rupees was made by the assessee to the same party on the security of the same property. The material terms of these deeds are that the rate of interest on the loan was to be 10 annas per cent. per month, that such interest was to be paid monthly, that in the event of simple interest for any consecutive period of 12 months remaining unpaid the borrower will have to pay compound interest at the rate of 10 annas per cent. for each month, that the borrower was to make payments at the rate of Rs. 7,500 per month, that such payments were to be credited in the first instance towards interest and the balance set off against the principal due and that in default of this payment the assessee creditor was to enter into possession of the property and, while in possession, to realise and receive the rents, etc.........and to apply the net rents, etc., remaining after paying and discharging all costs of realisation, etc...............firstly in paying themselves the monthly instalments of interest and secondly in applying the residue in and towards the reduction of the principal monies. In accordance with the terms of this agreement, the assessee took possession of the property in March 1932, that is, after the year of account with which we are here concerned and remained in possession for some time from that date.

4. Against the six lakhs of rupees principal advanced there was a payment of Rs. 80,000, in 1986-87 that is, the year prior to the year of account with which we are here concerned. The annual interest due for that year was Rs. 45,000 so that if this receipt had been dealt with in the manner directed in the mortgage deed, there would have been allocated a payment of Rs. 35,000 towards capital reducing the loan to Rs. 5,65,000 as at the beginning of 1987-88, while Rs. 45,000 would have been treated as interest accrued and actually received in that year (1986-87). Taking the principal outstanding at the beginning of 1987-88 as Rs. 5,65,000 the interest accruing on that sum in this year would be Rs. 42,375 and in that year the assessee actually received from the debtor Rs. 1,24,934 in all and in spite of the fact that the assessee appropriated the whole of the receipts in the year 1987-88 to capital, the Income Tax Officer allocated the sum of Rs. 42,375 to interest for that year and taxed it accordingly.

5. The assessee's case is that in view of the fact that the lease would expire in 1946 and the property would then revert to the original owner, he is not likely to be able to recover the whole of the principal advanced and that being the position he is justified

in allocating and entitled to allocate all payments towards the reduction of capital for the time being, while the Income Tax Officer has argued that the gross income from the property in question being about Rs. 1,20,000 though there may have been a fall in recent years on account of trade depression, while the expenses including rent to superior landlord, municipal taxes and repairs, lighting, etc., total only Rs. 47,200 there is a surplus of Rs. 72,800 for payment both towards interest and principal and therefore the assessee has no reason to assume that he will not get a return of the whole of the capital as well as a payment of the interest accrued before the expiry of the lease in 1946. It is true that the assessee in the year of account credited all payments made by the debtor against the principal of the loan made and has not applied these receipts or any portion of them in the first intance towards payment of the interest due though according to the mortgage deed, he was specifically bound to do so. It was alleged by the assessee before the Assistant Commissioner that he treated these receipts as he has done, in accordance with the subsequent agreement between him and the debtor but no evidence on that point was produced before the Assistant Commissioner. The assessee executed in December 1933 an agreement, appended hereto and marked C, with the debtor in which the history of this loan is narrated and in which it is further stated "as and from the date of taking possession......the mortgagees shall and will out of the monthly realisation.........apply the residue of the collection and rents towards the reduction of the capital money due ....and that after the liquidation of the principal money the residue of the gross rents.........shall be applied in and towards payment.........of the interest and compound interest accruing and accrued due and that interest shall be calculated in the same manner as is provided in the said two indentures of mortgage". This agreement of 1933, after stating how the interest was payable monthly with compound interest and when and why the mortgagees took over possession of the said mortgaged premises, recites that it was agreed that the mortgagees would, out of the realisations, pay the outgoings as provided for in the said indentures of mortgage and would apply the balance representing the net realisations towards reduction of the principal money bearing the accruing interest and compound interest in terms of the said indentures of mortgage, outstanding to be recovered after the satisfaction of principal money. The date of taking possession is March 1932 while the present assessment is one of the income of the account-

ending in June 1931 and it is amply clear that the assessee has not, as yet, waived his claim to the interest.

6. **Opinion of the Commissioner.**—I have set out the facts of the case above. The question on which I have been asked to state the case is "Whether it is open to a mortgagee notwithstanding a stipulation in the mortgage deed to apply payments, or in case when the mortgagee has taken possession the net realisation or realisations, with or without the consent of the mortgagor towards principal?" In so far the question refers to appropriation with the consent of the mortgagor it is sufficient to say that there is no evidence that the payments in question were appropriated towards the principal with the consent of the mortgagor. In fact no such consent was sought for or obtained; and in view of the terms of the mortgage and of the specific directions in the mortgage deeds themselves such consent cannot, in my opinion, be held to be implied. I have set out the relevant terms of the mortgage deeds. In view of the provisions for compound interest on outstanding interests it is clear that the direction for appropriation was for the benefit of the debtor and it was not therefore open to the mortgagee to disregard this express direction in the matter of appropriation of payments. Appropriation towards principal keeping the interest outstanding does not in the least benefit the mortgagor inasmuch as interest will run on the outstanding interest. It further appears that compound interest will be charged on the outstanding interest, and this will certainly make the position of the debtor worse if payments be not appropriated towards liquidation of the interest first. The appropriation in question was made by the assessee without any consent of the mortgagor, either express or implied, and in my opinion the question, in so far as it relates to the appropriation without the consent of the mortgagor, should also be answered in the negative. It is to be remembered in this connection that the assessee keeps his accounts on a mercantile basis and accrued interest is therefore legally taxable and apart from this, payments of an amount much greater than the interest accrued were actually made in the year of account, so that in fact we are taxing not merely accrued interest, but the interest which has both accrued and been paid.

The question further refers to appropriation of the realisations by the mortgagee when in possession. It may be pointed out here that so far as the present assessment is concerned it relates to a period before the mortgagee took possession and consequently in the facts and circumstances of this case that question would not

arise. But as I have been asked to state a case on such supposition as well I would submit that in view of the terms of the mortgage, realisations by the mortgagee in possession will stand on the same footing as payments made by the mortgagors so far as the question of appropriation is concerned.

7. I do not think Section 60 or 61 of the Contract Act has any applicability, for there are circumstances indicating to which debt the payment is to be applied (please see the mortgage deeds). The debtor gave his directions in the mortgage deeds themselves and the creditor is bound to apply the payments in the manner indicated in the said deeds. I think that the observations of the Judicial Committee of the Privy Council in the case of Maharaja of Darbhanga reported in 6 I.T.C. 401 (407) [*Commissioner of Income Tax, Bihar & Orissa* v. *Sir Kameshwar Singh*, 1933 I.T.R. 94] are of some assistance in determining the point at issue. There it is observed—"Now where interest is outstanding on a principal sum due and the creditor receives an open payment from the debtor without any appropriation of the payment as between capital and interest by either debtor or creditor the presumption is that the payment is attributable in the first instance towards the outstanding interest".

Here the case against the assessee is stronger still for the payment can hardly be held to be an open one in view of the specific stipulation in the mortgage deeds that all payments were to be credited in the first instance, towards interest. In my respectful opinion, therefore, the question as formulated above should be answered in the negative".

Dr. R. B. Pal for the Commissioner of Income Tax.

DERBYSHIRE, C.J.—Here the borrower is making payments to the lender under a mortgage deed at the rate of something over Rs. 7,500 per month. The mortgage deed stipulates that the rate of interest on the loan is to be ten annas per cent. per month, that such interest is to be paid monthly, that in the event of simple interest for any consecutive period of twelve months remaining unpaid the borrower will have to pay compound interest at the rate of ten annas per cent. for each month, that the borrower is to make payments at the rate of Rs. 7,500 per month, that such payments are to be credited in the first instance towards interest and the balance set off against the principal due and that in default of this payment the assessee creditor is to enter into possession of the property and, while in possession to realise and

receive the rents etc., and to apply the net rents etc., remaining after paying and discharging all costs of realization, *firstly*, in paying himself the monthly instalments of interest and *secondly*, in applying the residue in and towards the reduction of the principal monies. We are told that in accordance with the terms of this agreement the assessee took possession of the property in March 1932 and the question that has been propounded is this "whether it is open to a mortgagee notwithstanding a stipulation in the mortgage deed to apply payments, or in case when the mortgagee has taken possession, the net realisations of the mortgaged property towards interest, to appropriate such payments or realisations with or without the consent of the mortgagor towards principal?" We are concerned only with the first alternative, namely, before the mortgagee has entered into possession; we are not concerned with any other case; that is the only case that arises here. I think the principle to be applied has been laid down in the case of the *Maharaja of Dharbhanga* [1933 I.T.R. 94 at p. 103; 6 I.T.C. 401 at page 407] 'where interest is outstanding on a principal sum due and the creditor receives an open payment from the debtor without any appropriation of the payment as between capital and interest by either debtor or creditor, the presumption is that the payment is attributable in the first instance towards the outstanding interest." I think that principle is applicable to this case. But beyond that there is the definite stipulation in the mortgage deed that the money paid is to be appropriated, in the first instance, towards payment of interest and the balance set off against the principal due. It seems to me that what the mortgagee must do here is to apply the money received in accordance with the provisions of the mortgage deed. The income tax authorities are certainly entitled to assume that he is doing it. In my view there can only be one answer to the question with which we are concerned and the answer to the question is in the negative and the Commissioner of Income Tax will have the costs of these proceedings.

We have something to say about the form of the question as originally suggested by the petitioner in this case. Two questions were rolled up in the form of one question. We had endeavoured to answer it in the light of the facts stated in this particular case. We think that when questions are asked for our opinion one question should be asked at a time: an attempt should not be made to combine two or more questions in the form of one question. Further, the questions should not be divorced from the facts of

the particular case and should not be in the abstract as is the case here.

COSTELLO, J. :—I agree.

Reference answered accordingly.

[IN THE CALCUTTA HIGH COURT.]

In the matter of AMULYADHAN ADDY AND OTHERS.

SIR HAROLD DERBYSHIRE, C.J. and COSTELLO, J.

March 3, 1936.

ALLOWANCES—ASSESSMENT OF PROPERTY—INTEREST ON MORTGAGE—PROPERTY OF HINDU UNDIVIDED FAMILY—INTEREST PAID ON MORTGAGE EXECUTED BY SOME MEMBERS ONLY—*Busti* LANDS—INTEREST ON MORTGAGE CREATED FOR OTHER PURPOSES —WHETHER ALLOWABLE—INDIAN INCOME TAX ACT, (XI OF 1922), SECTIONS 9 (1) (iv), 12.

When the assessee is a Hindu undivided family and is being assessed in respect of income under the head 'property' under Section 9 of the Indian Income Tax Act, the word 'mortgage' in Section 9 (1) (iv) refers to a mortgage by the Hindu undivided family as such and does not also include a mortgage by any individual member or members of his or their shares only of such property.

In an assessment under Section 12 of the Indian Income Tax Act, for busti *lands the income is not to be computed after deducting the interest on the mortgages on such properties from the gross realisations in cases where the mortgages have not been made for any purposes of the said properties but for raising a loan for some other purposes of the assessee.*

Case stated by the Commissioner of Income Tax, Bengal, under Section 66 (2) of the Indian Income Tax Act in the matter of the assessment of Amulyadhan Addy and others a Hindu undivided family for the year 1933-1934. [Ref. No. 8 of 1935.]

STATEMENT OF CASE.

" At the request of the applicant, the two questions of law formulated in paragraph 7 of this statement of case are submitted to their Lordships, the Hon'ble Judges of the High Court, for favour of their decision.

2. FACTS OF THE CASE.—This matter arises out of an assessment made for the year 1933-34 on the income of the assessee from a business in paddy and rice, from moneylending, from income from property (assessed under Section 9 of the Act) from ground rent and from dividends, the accounting year being 1939 Akshoy Tritia year ending on some date in April 1932.

3. The Income Tax Officer in the assessment proceedings computed a total assessable income as below.

	Rs.
Property ...	... 12,693 (taxable under Section 9)
Busti land (Section 12) ... (Income from rent from ground the buildings whereon do not belong to the assessee).	22,122
Rice and paddy business at 78, Chetla Road, Calcutta ...	... 2,178
Rice and paddy business at 74, Chetla Road, Calcutta...	2,384
Dividends ...	... 126
Total	... 39,503
Less loss in money-lending business ...	... 351
Total income	39,152

While the Assistant Commissioner on appeal reduced the assessment in some immaterial particulars and computed an income as below

	Rs.
Property	... 12,693 (taxable under Section 9)
Business	... 1,777
Other sources (Section 12)	22,068
Total	... 36,538

4. The assessee, a Hindu undivided family governed by the Dayabhaga School of Hindu Law, had at some earlier date taken a loan from Raja Janakinath Roy on the security of part of his house property, his busti land, his share in an agricultural estate, certain holdings in stocks and shares and his stock-in-trade in his paddy

and rice business and at a later date had borrowed money from the Bhowanipore Banking Corporation, Ltd., on the same security, at a rate of interest of 9 per cent. Later still certain members of the assessee Hindu undivided family with a 12 annas interest in the family property had executed a third mortgage in favour of the Khulna Loan Company, giving in security their share in five separate house properties hitherto unmortgaged. It is to be noted that only 12 annas interest in this property was mortgaged and that the 4 annas share did not come in as he secured his share of the amount necessary to meet the creditors from his own individual property or from the family of his wife.

5. In the year of account the amount paid or payable on the first two mortgages by way of interest was Rs. 42,917 and the amount of interest paid or payable on the third mortgage was Rs. 7,236.

6. In the assessment the amount of interest of Rs. 7,236 on the third mortgage as stated above has been altogether disallowed as a deduction, while the interest of Rs. 42,917 on the first two mortgages has been allocated to the respective properties mortgaged, Rs. 7,716 being allocated to the *busti* lands, and the amount thus allocated to the *busti* lands has not been allowed as a deduction as the income derived from that property has been assessed under the head " Other sources " (Section 12 of the Income Tax Act), and as, according to the Income Tax Officer, that section does not admit of any such allowance.

7. The two relevant questions formulated by the assessee for reference to the High Court run as follows :—

(1) " Whether the deduction for interest on mortgage under Section 9 (1) (iv) is allowable in all cases of mortgage or only when a mortgage is created by all the co-owners of the property ?

and (2) Whether in an assessment under Section 12 for busti rents the real income as computed after deducting mortgagee's share of income, otherwise interest on mortgage, or the gross realisation from the source is to be taken for income ?"

As these two questions do not appear to me to be happily phrased I do not refer them to the Hon'ble High Court in that form but refer the following two questions in their stead :—

" (1) When the assessee is a Hindu undivided family and is being assessed in respect of income under the head 'Property' under Section 9 of the Income Tax Act, whether the word 'mortgage' in Section 9 (1) (iv) refers to a mortgage by the Hindu

undivided family as such or whether it includes also a mortgage of his share only of such property by any individual member thereof for his own purposes?"

(2) "Whether in an assessment under Section 12 for *busti* lands the income is to be computed after deducting from the gross realisations, any interest on mortgage of such properties such mortgage having been made not for any purposes of the said properties but for raising a loan for some other purposes of the assessee?"

8. **Opinion of the Commissioner.**—My own opinion on question (1) which I respectfully submit is as follows:—Under Section 9 (1) (iv) of the Act where the property is subject to a mortgage or other capital charge, an allowance is to be made in respect of the amount of any interest on such mortgage or charge. In my view, an allowance cannot come within that clause unless the interest is payable by the assessee (in this case, the Hindu undivided family) and in the present case the interest is not so payable but payable only by certain members of the family. No part of the mortgage money is payable by the undivided family as such and if the undivided family be taken as a separate entity distinct from its constituent members, as I think it must, for income tax purposes, then if the family as such is not liable to pay it should not also be able to claim any deduction on this account. Further, it is to be borne in mind that what is assessed under Section 9 of the Act is the *bona fide* annual value of property and the principle underlying that section appears to be that we should take the figure which can reasonably be accepted to be the income of the assessee on this account and in calculating this figure to make allowances for such interest on mortgages as may have to paid out of these probable annual realisations. This calculation has no concern with the selling value of the property and consequently the amount of interest on a mortgage effected by individual members of their shares in the property will not have to be paid out of the probable annual realisations of the family and so no allowance can or should be made for such interest under Section 9 (1) (iv) of the Act. In my respectful opinion therefore, the correct answer to this question is that an allowance is to be made in respect of the interest on a mortgage or charge only when the mortgage or charge is created by all the co-owners of the property.

9. In raising question 2 the assessee does not claim that the interest in question will fall within Section 12 (2) and in fact the interest paid is not any expenditure incurred for the purpose of making or earning the income, profits or gains of the *busti* lands.

It is admitted that the loan for which the mortgage of these *busti* lands was made had nothing to do with the acquisition, maintenance, improvement or mangement of such properties and it was in no way connected with these properties. The contention of the assessee is that as soon as a property is mortgaged the realisations from that property no longer wholly belong to its owner the mortgagor. According to his contention a portion of the rents and profits legally belongs to the mortgagee on account of interest and the balance, if any, alone belongs to the mortgagor. As a general proposition of law his contention is, in my opinion, wholly untenable. A mortgage does not necessarily divert the income of the property either wholly or partially to the mortgagee. The property is only a security for the repayment of the loan and nothing else.

In some special cases the mortgagee might be given some interest in the rents and profits. But in the present case the mortgage is a simple one and it is not contended that the mortgagee, as of right, could have appropriated any portion of such rents and profits. No portion of the rents and profits of the property was in any way assigned to the mortgagee and in my opinion it is idle to suggest that the whole realisations did not legally belong to the assessee. In fact the rents and profits were wholly realised by the assessee and they showed this realisation in their return. The income was their income, and it does not matter how they ultimately spent the same. As an expenditure it might have been an allowable deduction only if it were of the description of expenditure allowable under the relevant sections.

10 (*a*). It is an accepted principle of fiscal law that if an assessee claims any sum as an admissible deduction from taxable profits, the onus is on him to prove that the sum so claimed is an admissible deduction. Now, if we contrast Section 9 of the Act with Section 12, we find that the former section specifically provides for the allowance of such a claim. There is no such provision in Section 12 and the inference is that it was not intended that such a claim should be allowed.;

10 (*b*). The sum of Rs. 7,716 allocated against income from mortgaged *busti* land taxable under Section 12, was not allowed as a deduction from income under that head, as there was no evidence from which it could be shown or even inferred that the expenditure was necessary for earning the income, profits or gains sought to be assessed under that section and indeed the assessee's representative admitted at the time of assessment that the loan in question was not raised for the purpose of purchasing that *busti* land but for the

purpose of purchasing other land or constructing buildings on other properties. Under that section the income, profits and gains are to be computed after making allowance for any expenditure (not being capital expenditure) incurred solely for the purpose of making or earning such income, profits or gains. In this case, even if this mortgage had been incurred for the purpose of acquiring capital to purchase the property I am doubtful if the interest paid on that loan would even then have been an admissible deduction, for, in my view, the expenditure would, even in that case, have been incurred not for the purpose of making or earning the income, but for the purpose of acquiring the capital assets from which the income was subsequently derived. But here it is not contended that the loan in question was raised either for acquiring or improving the assets, from which this income taxable under Section 12, is earned.

11. It is respectfully urged that this question should be answered in favour of the revenue.

12. The assessee has formulated a third question, but as I propose to deal with that matter under Section 33 of the Act, I will not trouble their Lordships with it.

13. It is respectfully requested that a copy of their Lordships' decision may be forwarded to me in due course."

Mr. Sen, for the assessees.

R. B. Pal, for the Commissioner of Income Tax.

JUDGMENT.

COSTELLO, J.—The two questions on which we are asked to express our opinion have arisen in connection with an assessment made in the year 1933-34 on the income of the assessee derived from business in paddy and rice, and in money lending; and on income derived from properties assessed under Section 9 of the Indian Income Tax Act, XI of 1922, and from ground rents and dividends. There is also an item in the assessment which is described *busti* lands. That was assessed under Section 12 of the Indian Income Tax Act of 1922. The assessee is a Hindu undivided family governed by the Dayabhag School of Hindu Law. At some date long anterior to the date of the assessment that family had taken a loan from Raja Janaki Nath Roy on the security of part of the house property, *busti* land, and share in an agricultural estate, certain holdings in stocks and shares and the stock-in-trade in the paddy and rice business. On a subsequent date the family had borrowed money from the Bowanipur Banking Corporation

Ltd., on the same security at a rate of interest of 9 per cent. Some time after that certain members of the Hindu undivided family which constitutes the assessee—these members having a twelve annas interest in the family property—executed a third mortgage in favour of the Khulna Loan Company giving as security their share in five separate house properties at that time not subject to any mortgage. As the learned Commissioner of Income Tax points out it should be noted that only 12 annas interest in these properties was mortgaged and the other sharer, the four annas sharer, did not come in at all as he raised his share of the amount necessary to meet their creditors from his own individual property or that of his wife's family.

In the year of accounting the amount paid or payable on account of the first two of the mortgages I have mentioned by way of interest was the sum of Rs. 42,917 and the amount of interest paid or payable in respect of the 3rd mortgage was Rs. 7,236. In the assessment the amount of interest of Rs. 7,236 in respect of the 3rd mortgage has been disallowed altogether, that is to say, the Income Tax Officer has declined to allow it to be treated as a deduction. The sum of Rs. 42,917 being the amount of interest on the first two mortgages has been allocated to the respective properties mortgaged, Rs. 7,716 being allocated to the *busti* lands and this amount has not been allowed as a deduction because the income derived from the *busti* lands has been assessed under the head "other sources," that is to say under the provisions of Section 12, of the Indian Income Tax Act. The Income Tax Officer took the view that that section does not admit of any such allowance.

Certain questions were formulated by the Assessee for reference to this court. They were in extremely general terms and, as the learned Commissioner of Income Tax himself has said, they do not appear to be happily worded and accordingly he declined to refer them to this court in their original form. He substituted in their place two other questions which are the questions we have to answer. They are these: (1) "When the assessee is a Hindu undivided family and is being assessed in respect of income under the head 'property' under Section 9 of the Income Tax Act, whether the word 'mortgage' in Section 9 (1) (iv) refers to a mortgage by a Hindu undivided family as such or whether it includes also a mortgage of his share only of such property by any individual member thereof for his own "purposes"? (2) Whether in an assessment under Section 12, for *busti* lands the income is to be computed after deducting from the gross realisa-

tions, any interest on mortgage of such properties, such mortgage having been made not for any purposes of the said properties but for raising a loan for some other purposes of the assessee." In order to give answers to these two questions it is desirable to refer at the outset to two of the definitions which are contained in Section 2 of the Indian Income Tax Act of 1922. Sub-Section 2 of Sections 2 reads thus: 'Assessee' means a person by whom income tax is payable, and sub-Section 9 reads thus—'Person' includes a Hindu undivided family. In the previous Income Tax Act (of the year 1918) those two sub-Sections were all contained in sub-Section (2) of Section 2 of that Act, which accordingly read thus—'Assessee' means a person by whom income tax is payable and includes a firm and a Hindu undivided family. Although in the present Act, assessee in one place is defined as a person by whom income tax is payable and in another place "p erson" is stated to include a Hindu undivided family, the effect is the same as that of the definition in the Act of 1919. Putting the two things together for our present purpose it comes to this that the assessee with whom we are concerned is a Hindu undivided family. So much has been admitted by Mr. Sen appearing on behalf of the Assessee.

Mr. Sen has argued as regards the first of the two questions we have to answer that by reason of the provisions in Section 9 (1) (iv) the position in the present case is that the property is subject to a mortgage—the property which is the basis of the assessment under Section 9 (1)—and that therefore the assessee is entitled to claim as a deduction the amount of interest which is payable in respect of the mortgage on a part of the property even though that mortgage was effected not by the undivided joint Hindu family as such but only by some of the co-sharers who constitute that undivided family. That contention seems to me to ignore the fact that the Assessee is the undivided Hindu family—not the persons who compose that family but the family taken as a unit; in other words the undivided Hindu family is a single unit for the purpose of income tax matters. In that view of the position to say that merely because certain part of the property had been mortgaged or because persons having a twelve annas share in the family property executed a mortgage or mortgages and therefore interest payable in respect of those mortgages is a deductible allowance is to read into Section 9 (1) (iv) words which are not there and to make the Section read something like this; "where property *or any part of* the property was subject to a mortgage" &c. I

am clearly of opinion that Section 9 (1) (iv) of the Act applies only when *the* property, that is to say, *the* property which constitutes the taxable property of the undivided Hindu family is subject to mortgage. That is not the position here.

The result is that as regards the first question we are bound to say that when the assessee as a Hindu undivided family is being assessed in respect of his income under the provisions of Section 9 of the Income Tax Act, the word "mortgage" in Section 9 (1) (iv) refers to a mortgage by the Hindu undivided family as such and does not also include a mortgage by any individual member or members of his or their shares only of such property.

As regards the second question Mr. Sen has conceded that the mortgages that were made in respect of the *busti* lands were not such as would fall within the purview of Section 12 (2) of the Income Tax Act. That sub-section says "such income, profits and gains" that is to say income, profits and gains referred to in Sub-Section (1) shall be computed after making allowance for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making or earning such income profits or gains, provided that no allowance shall be made on account of any personal expenses of the assessee." It is obvious that the interest payable in respect of the mortgages on the *busti* lands cannot by any stretch of language be accurately described as expenditure incurred solely for the purpose of earning the income which is derived by the joint Hindu family from the *busti* lands.

The learned Commissioner has pointed out in the statement of the case that the contention of the assessee was that as soon as a property is mortgaged the realisations from that property no longer wholly belong to its owner the mortgagor. According to his contention a portion of the rents and profits legally belongs to the mortgagee on account of interest and the balance, if any, alone belongs to the mortgagor." The learned Commissioner has expressed the view that as a general proposition of law this contention is wholly untenable. With that expression of opinion I entirely agree. It is manifest that rents and profits or proportionnate rents and profits derivable from the *busti* lands were in no sense earmarked or allocated for the purpose of paying interest due in respect of the mortgages on those *busti* lands. It was open to the mortgagor to discharge his liability for interest by using either part of the rents and profits derived from the mortgaged *busti* lands or by using any other resources if he was so

minded. There is nothing whatever to show that the interest payable in respect of the mortgages on the *busti* lands was paid out of the rents and profits received by the mortgagor from those particular lands.

It follows therefore that the answer to the second question must be this that in an assessment under Section 12 of *busti* lands the income is not to be computed after deducting the interest on the mortgages on such properties from the gross realisation in cases where mortgages have not been made for any purposes of the said properties but for raising a loan for some other purposes of the assessee.

The Income Tax Department will get such costs of the reference as are allowed by the rules.

DERBYSHIRE, C. J.—I agree.

Reference answered.

[IN THE PRIVY COUNCIL].

RM. AR. AR. RM. ARUNACHALAM CHETTIAR

v.

COMMISSIONER OF INCOME TAX, MADRAS.

LORD BLANESBURGH, SIR SHADI LAL and SIR GEORGE RANKIN.

February 27, 1936.

INCOME TAX—PARTNERSHIP—UNREGISTERED FIRM—PARTNER'S RIGHT TO SET OFF SHARE OF LOSS OF FIRM AGAINST HIS INDIVIDUAL PROFITS AND GAINS—SOLVENT PARTNER—CLAIM TO SET OFF INSOLVENT PARTNER'S SHARE OF LOSS AS LOSS IN BUSINESS OR BAD DEBT—PERMISSIBILITY—ASSESSMENT OF FIRMS —DUTIES OF INCOME TAX OFFICERS—SCHEME OF INDIAN INCOME TAX ACT—INDIAN INCOME TAX ACT (XI OF 1922), SECTIONS 6, 14 and 24.

Whether a firm is registered or unregistered, a partner's share of the loss in the firm can be set off against the profits and gains made by him in his individual trade and otherwise. But a partner cannot claim to deduct against other profits or gains a sum which he has become liable to bear or pay by reason that he has paid or will have to pay on account of the firm more than his share so as to give him a right of contribution from the other partner who is

insolvent. Though logically the whole of the loss may in a case like this fall upon the solvent partner and not merely his proper share of the loss, different considerations arise for income tax purposes. A partner in a continuing partnership cannot at the end of any year's trading claim to set off the whole of the firm's loss in the previous year treating the other partner as insolvent. He is not entitled to do so on the dissolution of the firm, nor can he later, according as the other partner's insolvency becomes established, set off in one year the whole of such partner's shares of loss for several years. No principle of writing off a bad debt could justify such a course whether in the year following the dissolution or in some subsequent year in which the partner's insolvency has crystallised.

The kind of account which is necessary between partners to settle questions and claims between them is beyond the scope of an Income Tax Officer's investigation. His duty is to compute properly the profits made my the firm or the loss incurred by the firm and for this purpose he has no occasion to embark upon the computation of the exact value of any partner's interest in the capital or the details of the partner's accounts in the firm's ledger. He has only to enquire what is each partner's share.

The basis of the system of double assessment adopted by the Indian Income Tax Act is that the individual partner is chargeable on his share of the firm's profits regardless of all questions whether he actually receives it as income paid to him or whether under the articles of partnership he is entitled to draw it out.

The assessee was the sole owner of a money-lending buiness and the capitalist partner in a cotton business with another person S. The cotton business did not prosper and was closed down on the 31st March, 1930. In the partnership accounts the share of each partner in the loss was shown separately. As S was a man without any means, the assessee had to bear the entire loss in the cotton business. On 1st April, 1930, the debit against S in the partnership accounts was accordingly transferred to the assessee's money lending accounts and in March, 1931, the debit against S was written off as a bad debt. In calculating the taxable income of the assessee for the year ending March 1931 the assessee claimed that in addition to his share of the loss incurred by the firm the amount thus written off should be set off against his income from the money lending business. Held, *that the assessee was not entitled to have this amount set off against his income either as loss in business or as bad debt. From before the moment at which this*

debt was transferred from the cotton business to the money-lending business it was altogether bad. It could not therefore be considered as a bad debt made by the assessee in the course of his money-lending and still less could it be considered as having become bad in the year of account.

COMMISSIONER OF INCOME TAX, MADRAS *v.* RM. AR. AR. RM. ARUNACHALAM CHETTIAR (1934 I.T.R. 401) *affirmed.*

Cases referred to:

NEEMCHAND DAGA, *In re* [1931] (I.L.R. 58 C. 1204; 134 I.C. 931; A.I.R. 1931 Cal. 686; 35 C.W.N. 534).

COMMISSIONER OF INCOME TAX, MADRAS *v.* ARUNCHALAM CHETTIAR [1924] (I.L.R. 47 Mad. 600; 77 I.C. 772; A.I.R. 1924 Mad. 474).

RICHARDSON *v.* BANK OF ENGLAND [1838] (41 R.R. 49; 8 L.J. N.S. Ch. 1).

Appeal from a decision of the Madras High Court, dated May 1, 1934, reported as 1934 I. T. R. 401.

S. Hyam and *J. E. Godfrey*, for the appellant.

Gavin Simonds, K. C. and *W. Wallach* for the respondent.

JUDGMENT.

SIR GEORGE RANKIN.—This is an appeal by the assessee from the decision of the High Court at Madras on a reference made by the Commissioner of Income Tax, Madras, under Section 66 (2) of the Indian Income Tax Act (Act XI of 1922). The appellant is the manager of the Hindu undivided family and the order of assessment dated March 11, 1932, was in form an assessment to income tax of the Hindu undivided family. The year of assessment is the year 1931-32 and the year of account is the previous year, *viz.*, 1930-31. The appellant took exception to the assessment made by the Income Tax Officer on March 11, 1932, as aforesaid, but his appeal to the Assistant Commissioner of Income Tax was on December 10, 1932, dismissed and the High Court of Madras has in effect upheld the orders of the income tax authorities.

The facts of the case as stated by the Commissioner and as appearing by the orders of the Assistant Commissioner and Income Tax Officer [extracts from these orders being exhibited to the letter of reference] are as follows. The appellant [for this purpose he will be referred to as an individual] carries on a money-lending business in various places and in addition is possessed of property at various places and of dividends, all of which are subject to Indian income tax. At a place called Perambalur he carries on two

business, one of which is a business of money-lending, and prior to March 31, 1930, he had also carried on, but in partnership with one A. Somasundaram Pillai, a third business in the purchase and sale of cotton. This business had been started in 1926, the respective shares of the appellant and Pillai in both profit and loss being 5/8ths and 3/8ths. It appears that Pillai was a working partner, a man of little or no means: there does not appear to have been any written agreement of partnership, and neither party undertook to bring any capital into the partnership in the strict sense of this expression—that in the sense in which the word is used in clauses (*c*) and (*d*) of Section 13 of the Indian Partnership Act (IX of 1932). The money necessary for purchasing cotton and carrying on the business was provided by the appellant on the terms that interest was to be paid upon his advances. In the books of his money-lending business at Perambalur these advances were debited to the cotton partnership. It is not clear how far interest was actually paid in any particular year, but interest was charged and was entered in the books of both businesses. The cotton business was started in the year 1926, but there is not in evidence any statement of the profits or losses of each year, nor of the details of the interest account in the books of the money-lending business. It it clear, however, that the accounts of the cotton partnership were made upon the footing that it was liable to pay interest in respect of the advances. The business was a losing one. Accounts were first settled between the partners on March 31, 1928, with the result that Pillai's share of the loss up to that date was found to be Rs. 9,396 and the appellant's Rs. 15,660. Thereafter the business incurred further losses and when it was discontinued as at March 31, 1930, Pillai's share of the further losses was Rs. 20,268 and the appellant's Rs. 33,780. Pillai's share of loss debited to his account in the partnership books on March 31, 1930 was with interest Rs. 34,069.

The appellant in his assessment for the year 1928-29 was allowed to deduct his share of the loss in this cotton partnership. This presumably refers to the loss made in the year 1927-28. It would seem that the appellant in the year of assessment 1930-31 was allowed to deduct for income tax purposes his share of the rest of the partnership losses. In this way 5/8ths of the total losses of the firm have in due course been deducted from his other profits This was doubtless done in accordance with the ruling gived by the Madras High Court in the case of *Commissioner of Income Tax, Madras* v. *Arunachalam Chettiar* where it was held that a partner

in an unregistered firm which has made a loss in the year of account is entitled to set off his share of the loss against the profits and gains made by him in his individual trade and otherwise. At no time before the year of assessment with which we are now concerned (*viz.*, 1931-32) does it appear that any attempt was made by the appellant to claim that his partner Pillai being unable to meet any share of the firm loss, the appellant, for purposes of income tax could claim to deduct from his other profits any greater share than 5/8ths of the losses of the cotton firm. In particular, although the cotton business was closed at the end of the year 1929-30, *viz.*, on March 31, 1930, no such claim was made in respect of the year of assessment 1931-32 for which assessment the last year of the cotton business was the year of account.

What happened after March 1930, was as follows. On April 1, 1930, the debit against Pillai in the books of the cotton partnership was transferred to the account of the appellant's money-lending business at Perambalur. The meaning of this transfer and its justification invite comment which may be postponed for the present. On September 29, 1930, a further debit was made to this new account of Rs. 2,569 by way of interest, bringing the total debit to Rs. 36,638. On this date Pillai gave to the appellant a promissory note for this amount, and a fresh folio was opened in the books of the appellant's money-lending business styled "A. Somasundaram Pillai, Promissory Note Account". On March 28, 1931, the appellant took from Pillai a mortgage of certain house property for Rs. 500. On March 31, 1931, that is on the last day of the year of account with which the present assessment is concerned, the appellant wrote off the balance Rs. 36,138 as a bad debt.

In his assessment for 1931-32 the appellant claimed to deduct the above sum of Rs. 36,138 from the amount of the profits of his money-lending business at Perambalur for the year 1930-31. It would seem that apart from this deduction the money-lending business in the year of account made a loss, but the appellant in that year had other taxable profits.

The income tax authorities, supported by the High Court of Madras, have disallowed this claim, which in form, as already shown, was a claim to have an allowance in respect of a bad debt made in the year of account by the money-lending business at Perambalur. The question which the appellant desired the Commissioner to refer to the High Court was framed by him as follows :—

"Whether the debt of A. Somasundaram Pillai written off as an irrecoverable loan in the year of account is not

liable to be deducted from the assessee's income for the year ?"

The Commissioner being of opinion that in fact no loan was ever made by the appellant's money-lending business at Perambalur to Pillai, refused to state the question in this form, but referred for the decision of the High Court the following question :—

"Whether the ex-partner's share of the loss in the cotton trade which the petitioner had to bear by reason of the ex-partner being unable to meet his share of loss in the partnership business, can be set off against the petitioner's other income, profits or gains as a loss of profits or gains within the meaning of Section 24 of the Act."

Upon this question, so referred as being the real question which arises in the case, the Commissioner gave as his opinion that as Pillai had no capital, the appellant had to meet the loss from the capital contributed by him to the cotton partnership and that the loss claimed to be deducted was a loss of capital and not a loss of profits or gains within the meaning of Section 24.

The learned Chief Justice of the High Court at Madras, with whom the other Judges agreed, answered the question referred in the negative, holding that in the books of the cotton business there was nothing to show that the appellant had made any other or further loss in that business than his five-eighths share, and that as the money-lending business never lent any money to Pillai but only to the cotton partnership Pillai never became a debtor of the money-lending business at all.

As it is reasonably clear that Pillai, who is described by the learned Chief Justice as "a man of straw" was at no material date possessed of any capital, it will be convenient to consider the question pronounced by the Commissioner first of all from the point of view of the appellant as at the time when the cotton business was closed down. It appears to their Lordships to be reasonably clear that in respect of five-eighths of the loss made by the cotton partnership in its last year of trading, namely 1929-30, the appellant in the year of assessment, 1930-31, was entitled to claim a deduction from his other income. The same is true *mutatis mutandis* in respect of previous assessment. Their Lordships fully approve of the decision in the case already cited, *Commissioner of Income Tax, Madras* v. *Arunachalam Chettiar*, and of the reasons given in the judgment of SCHWABE, C. J., for so holding. In particular they are of opinion that the learned Chief Justice rightly rejected the contention put forward in that case, that an unregist-

ered firm was for income tax purposes an "entity" or that the same person as an individual and as a partner of a firm is two separate "entities", merely because the business of the firm is a separate business, and the firm is treated as an assessee. From Section 24 (2) of the Indian Income Tax Act it would seem that the Indian legislature thought it necessary to anticipate any possible apprehension that a partnership, by being registered as a registered firm within the meaning of Section 26 of the Act, might be treated as a separate assessee in so absolute a sense as to prevent a partner's share of loss being set off against his individual profits or gains. In their Lordships' opinion whether a firm is registered or unregistered, partnership does not obstruct or defeat the right of a partner to an adjustment on account of his share of loss in the firm, whether the set off be against other profits under the same head of income within the meaning of Section 6 of the Act or under a different head [in which case only need recourse be had to Section 24 (1)]. So long as the set off is of his share of the loss made by the firm in the year of account, the adjustment does not involve the taking of any general or other account between the partners or indeed any examination of the accounts of the individual partners in the books of the firm. No question of the amounts paid by individual partners on the firm's behalf or of the right of one partner to contribution from another complicates the calculation which is based (*a*) upon the amount of profit or loss made by the firm as a firm, and (*b*) on the share or fraction attributable to each partner by the agreement of partnership between them.

If, however, a partner can claim to deduct against other profits or gains a sum which he has become liable to bear or pay (*a*) by reason that he has paid or will have to pay on account of the firm more than his share, (*b*) so as to give him a right of contribution from the other partner, (*c*) who is insolvent, the character of the investigation to be made is entirely altered. Logically, it may perhaps be said, the whole of the loss of the last year of trading at least is in a case like the present falling upon one partner and not merely his proper share of the loss. But for income tax purposes very different considerations arise. As the appellant on the conclusion of the last year of trading did not in his character of partner formulate any claim to a deduction of more than five-eighths of the loss in the cotton business, it is necessary now, if the question stated by the Commissioner is to be answered, to formulate precisely the further claim which is under discussion. Is the sugges tion that at the end of any year's trading one partner in a continuing

partnership, treating the other as insolvent, can claim to set off the whole of the firm's loss in the previous year? Or is it that he can do so on the dissolution of the firm? Or that later, according as the other partner's insolvency becomes established he can set off in one year the whole of such partner's share of loss for several years? Looking at the matter as a question of what a partner in a firm may claim to deduct from his other income, their Lordships are not of opinion that in any of these forms the claim can be regarded as permissible.

In one year a partner may draw out more, in another year less, than his share of profits. In one year a partner may have expended money on behalf of his firm; in another year another partner may have done the like. Questions may arise, regardless of whether the firm has otherwise made a profit or loss, as to the firm's right to be indemnified by a partner for loss caused to it by his wilful neglect, (*cf.*) Indian Partnership Act (No. IX of 1932), Section 13 (*e*) and (*f*). Between partners any right of contribution has reference, *prima facie*, at least to the ultimate balance appearing as the result of a general account. For this purpose let all questions of mere procedure for the enforcement of a partner's right be disregarded, and let the money owing from one partner to another be treated as in equity a debt. Whether the old rule as stated by LORD COTTENHAM in *Richardson* v. *Bank of England* that "pending a partnership equity will not interfere to set right the balance between the partners", is still to be adhered to rigidly or not, the kind of account which is necessary between partners to settle questions and cross-claims between them is beyond the scope of an Income Tax Officer's investigation. His duty is to compute properly the profits made by the firm or the loss incurred by the firm. For this purpose he has no occasion to embark upon the computation of the exact value of any partner's interest in the capital or the details of the partner's account in the firm's ledger. He has only to enquire what is each partner's share. The firm is considered as doing business with third parties. For the present purpose individual partners are not to be considered as trading with or doing business with each other but as having shares in the profit or loss of the firm. On any other principle profits made by the firm may go untaxed and losses made by the firm may be allowed for more than once. The present case may be quite free from complication. But that the claim now in question clashes with the principles of the Indian Income Tax Act will be apparent from an examination of the statute.

Under the Act both the firm and the individual partners have to make returns and are assessed whether the firm is a registered firm or not. This principle or practice, for it is both, has sometimes been referred to as the principle of "double assessment" and was much discussed in the case of *In re Neemchand Daga.* An unregistered firm is treated as an individual both as regards rate of tax and as regards super-tax. The registered firm on the other hand pays income tax at the maximum rate in all cases independently of the amount of its total profits, but is not assessed to super-tax at all. In neither case does the individual partner have to pay again on his share of profits if the tax has already been assessed on the firm (Section 14 (2) (*b*)). Moreover, in the case of the registered firm by the operation of Section 48 the individual partner may obtain a refund of tax paid on his share if the rate at which he is chargeable to tax as an individual is not maximum rate. This full procedure, however, is not always followed in the cases of registered firms: in order to avoid unnecessary payments and unnecessary proceedings for a refund, the partner is sometimes taxed directly on his share at the rate ultimately payable by him. Now the basis of this system is that the individual partner is chargeable on his share of the firm's profit regardless of all questions whether he actually receives it as income paid to him or whether under the articles of partnership he is entitled to draw it out. Special stipulations between the partners may obstruct the partner's right in the year of account or at all to withdraw his aliquot portion of the total profits. All such matters are disregarded by the statute and save upon this principle the working of the Act could hardly proceed. That the tax is to be levied by reference (*a*) to the total profits of the firm, and (*b*) the particular partner's share in the profits, is manifest in Sections 14 (2) (*b*), 23A (1) and 4 (*i*), 26A, 48 (2) and 55.

It is in no way surprising, therefore, that in the only case in which express reference is made by the Act to the deduction which an individual partner may make from his other income in respect of his share of his firm's loss—the case, namely, of a registered firm—the same principle should be recognised. The words used in Section 24 (2) are "Any member of such firm shall be entitled to have set off...such amount of the loss...as is proportionate to his share in the firm." The phrase "share in the firm" is not beyond criticism as it ignores the fact that however usual it is not actually necessary that the aliquot portion or interest of a partner should be the same in profits as in losses, but no reasonable doubt

can exist that the measure of this right of set off, in the case of a registered firm, is given by the phrase. Both upon principle and as a matter of construction of the statute, the alternative in the case of an unregistered firm is between holding that the right of set off does not arise and holding that it is a right of the same character and measure to be worked out in the same way. After all, even if a partner is insolvent, he may nevertheless have had in the year of account income from other business or sources against which his share of the firm's loss can be deducted for purposes of income tax. If *B* may get credit for his share of the loss, there is at least a formidable difficulty in the way of giving credit to *A* for the whole. That persons without capital should be taken as partners in a business is doubtless, at times both reasonable and desirable, but it is not clear that this would be unduly discouraged merely because in case of loss the capitalist partner might be better off if by the partnership articles in accordance with reality he took the whole responsibility for losses.

Their Lordships moreover can give no countenance to a suggestion that upon a dissolution of partnership a partner's share of the losses for several preceding years can be accumulated and thrown into the scale against the income of another partner for a particular year. No principle of writing off a bad debt could justify such a course, whether in the year following the dissolution or, as logic would permit, in some subsequent year in which the partner's insolvency has crystallised. The "bad debt" would not, if good, have come in to swell the taxable profits of the other partner. In the present case the claim to set off is in fact made in the second year of assessment after the dissolution of the business. It has already been observed that the scheme of the statute is not to treat partner *A* as if in connection with the firm's affairs he was trading *vis-a-vis* *B*, or doing business with *B* as the other party. Still less can it properly be held that years after the dissolution of the business *A* is doing business with *B* and making good debts or bad debts due from him. Their Lordships are accordingly of opinion, that the question propounded by the Commissioner of Income Tax has been rightly answered by the High Court of Madras in the negative.

It remains, however, to note that the appellant in the year 1930-31 took steps to give another character to his partner's share of the losses made in the cotton business between 1926 and 1930. As the Income Tax Officer put it "on April 1, 1930, the debit against A. Somasundaram Pillai in the accounts of the partnership

was transferred to the petititioner's money-lending business." On September 29, 1930, interest of Rs. 2,569-6-0 was added, bringing the total amount of Rs. 36,638-4-9. On the same day, September 29, 1930, the appellant took a promissory note from Pillai and on March 28, 1931, took a mortgage deed for Rs. 500. On March 31, 1931, he wrote off as bad the sum of Rs. 36,138-4-9. These steps can only have been taken in order to found a claim that in the year of account 1930-31, the appellant had made a loss in his money-lending business. But this claim was rejected by the Commissioner on the short ground that no loan was as a matter of fact advanced by the appellant's money-lending business to Pillai though it is true that the appellant advanced monies to the cotton partnership. Their Lordships have the greatest difficulty in seeing how the circumstance that the appellant carries on business as a money-lender can affect his rights in respect of advances made to his own firm. It is no part of the business of a money-lender to finance the money-lender's ventures in the cotton market. Conversely, it is not a sign or index of the money-lender that one advances money to one's own firm. The basis of the right to deduct irrecoverable loans before arriving at the profit of money-lending is that to the money-lender, as to the banker, money is his stock in trade or circulating capital: he is dealing in money. But a solvent man can hardly make a loss by lending money to himself even if another be made responsible for the loan as well. And when the loan is in reality but a putting of the hand into the pocket to pay for cotton, it seems desirable to ask what is the real equity between the parties. Their Lordships think that a reference to Sections 24 and 44 of the English, and Sections 13 and 48 of the Indian, Partnership Acts provides a correct answer and that the true and ultimate right of the appellant against Pillai was a right to contribution in proportion to the *latter's* share of profits. This is none the less true that the money was not put up by way of partner's capital. Even if three-fifths of the money can also be regarded as in equity a loan to Pillai, it is very far from being money lent in the course of business as a money lender, as is shown by the equities affecting the right to be repaid.

When *A* purports to lend money to *A* and *B*, much may be done with the consent of *B*. The transfer of the entry to the debit of Pillai from the books of the cotton partnership to the books of the appellant's money lending business may in the circumstances of this case be taken as having been effected with the consent of Pillai. The element of novation, however, comes in too

late. Pillai's inability to meet his share of the loss was just as hopeless by the end of March 1930 as at any later time. The appellant's return for the year 1930-31 did not have to be rendered until months after March 1930, and if he filled in time by making entries in his books at the beginning and end of the year 1930-31, that delay does not entitle him to choose the next year for his claim to a set off. From before the moment at which this debt was transferred from the cotton business it was altogether bad and its badness was the reason of the transfer. It cannot, therefore be considered as a bad debt made by the appellant in the course of money-lending and still less can it be considered as becoming bad in the year of account, hence the process by which the transfer is made on the first day of the year 1930-31 and cancelled as a bad debt upon the last day of that year is of no avail to the appellant.

Their Lordships are not in any way disposed to criticise the decision of the Commissioner refusing to regard the transaction as an irrecoverable loan made in the course of a money-lending business. They think, however, that it would have been more convenient, and more strictly in accordance with Section 66 (2) of the Act, if the Commissioner had, after setting out the evidence upon this question and his findings thereon, stated and referred to the High Court the question of law, *viz.*, Whether it was open to him in law to hold that the loss in question was not a loss of profits or gains incurred by the appellant in the year of account by reason of an irrecoverable loan made in the course of his business as money-lender so as to entitle the appellant to have the amount thereof set off against his other income, profits or gains in the said year.

They will humbly advise His Majesty that this appeal should be dismissed. The appellant must pay the costs.

Appeal dismissed.

Solicitors.—Douglas Grant & Dold, for the appellant; *The Solicitor, India Office,* for the respondent.

[IN THE PRIVY COUNCIL.]

In the matter of THE FINANCE ACT (NORTHERN IRELAND).

LORD CHANCELLOR (VISCOUNT HAILSHAM), LORD THANKERTON, LORD MAUGHAM, SIR GEORGE LOWNDES and SIR SIDNEY ROWLATT.

March 27, 1936.

INCOME TAX—PURPOSES OF INCOME TAX ACTS—INCOME TAX AND POOR RATE—DIFFERENCE BETWEEN—FINANCE ACT (NORTHERN IRELAND) 1934, SECTION 3—PROVISIONS OF SECTION 3, IF BEYOND THE POWERS OF THE PARLIAMENT OF NORTHERN IRELAND.

Even assuming that under Section 3 of the Finance Act of 1934, (Northern Ireland) a tax is imposed on the ratepayers by the central authority, such tax is not substantially the same in character as income tax, and the provisions of Section 3 are within the powers of the Parliament of Northern Ireland.

The purposes of the Income Tax Acts is to tax a person's total income from all sources; the method of assessing income derived by ownership or occupation of hereditaments is somewhat arbitrarily based on annual value and not on actual income, but that does not alter the essential characteristic of income tax that it is a tax on income generally. On the other hand, the poor rate is levied in respect of the occupation of hereditaments, irrespective of a person's income generally, and irrespective of whether the ratepayer is in fact deriving profits or gains from such occupation. A dwelling house is a burden, not a source of profit for the occupier who pays rent for it. He is rated on the value of the burden, while he remains unrated in respect of his whole profits, be they from business or from investments. This marks the essential difference in character between income tax and rates. London County Council v. Attorney General (1901 A. C. 26).

Gavin T. Simonds, K. C., W. M. M. Graham Harrison, K. C., J. M. Whitaker and *J. C. MacDermott*, for the appellants.

The Attorney General for Northern Ireland, H. L. Murphy, K. C., and *J. Desmond Chambers*, for the respondent.

LORD THANKERTON.—In this reference under the provisions of Section 51 of the Government of Ireland Act, 1920, the matter to be determined is whether the provisions of Section 3 of the Finance Act (Northern Ireland), 1934, are beyond the powers of the Parliament of Northern Ireland.

Section 3 of the Finance Act of 1934, provides as follows:

"3.—(1) There shall be paid to the Exchequer of Northern Ireland by the Council of every county and county borough an annual contribution towards the cost to the said Exchequer of educational services.

"(2) The contributions to be paid by each such Council as aforesaid in respect of each financial year shall be as follows:—

"(a) in respect of the year ending on the thirty-first day of March, nineteen hundred and thirty-five, an amount equal to the sum which would be produced by a rate of six-pence in the pound on the rateable value of the county or county borough;

"(b) in respect of each subsequent year an amount equal to the sum which would be produced by a rate of one shilling in the pound on the rateable value of the county or county borough.

"The contribution to be paid by the Council of a county or county borough shall be raised by means of the poor rate, and shall so far as it represents a rate on the rateable value of a borough or other urban District, be raised by the Council of the borough or urban District upon the demand of the county Council.

"Where a Council, for the purpose of providing any sums required to be raised by them for the contribution to be paid in respect of the year ending on the thirty first day of March, nineteen hundred and thirty-five, borrow money temporarily in exercise of the powers conferred upon the Council by section three of the Local Authorities (Financial Provisions) Act, 1921 (or any similar enactment in a Local Act), the term within which such money is required to be repaid shall be a period not exceeding six months from the ending of the said year.

"The contributions payable under this section shall be paid in such instalments payable at such time as the Ministry of Finance may direct.

"Expenditure incurred by a Council in paying any contribution or meeting any demand under this section shall not be taken into account for the purposes of the deficiency contribution under Section 12, or Section 13 of the Local Government (Rating and Finance) Act (Northern Ireland), 1929, as amended by any enactment for the time being in force.

"(6). In this section the expression 'rateable value' means the rateable value, subject to the provisions of Part I of the said Local Government (Rating and Finance) Act, of the hereditaments and tenements rated to the poor rate for the financial year immediately preceding the year in respect of which the contribution is to be paid.'

The parties interested, who appeared before the board, were the Lord Mayor, Aldermen and Citizens of the City of Belfast (hereinafter called "the Corporation"), who challenged the validity of the section above quoted, and the Government of Northern Ireland, who supported the validity of the legislation.

The Corporation bases its challenge on the provisions of Section 21 (1) of the Government of Ireland Act, 1920, which provides as follows:

"21.—(1) The power of the Parliaments of Southern Ireland and Northern Ireland to make laws shall include power to make laws with respect to the imposing, charging, levying and collection of taxes within their respective jurisdictions, other than customs duties, excise duties on articles manufactured and produced, and excess profits duty, corporation profits tax, and any other tax on profits, and (except to the extent hereinafter mentioned) income tax including super tax, or any tax substantially the same in character as any of those duties or taxes, and the Government of Southern Ireland and Northern Ireland shall have full control over the charging, levying and collection of such taxes as their respective Parliaments have power to impose and the proceeds of all such taxes shall be paid into the Consolidated Fund of Southern Ireland or Northern Ireland, as the case may be.

Provided that it shall not be competent for the Parliament of Southern Ireland or the Parliament of Northern Ireland to impose any tax, whether recurrent or non-recurrent, of the nature of a general tax upon capital not being a tax substantially the same in character as an existing tax."

The Corporation maintains that under Section 3 of the Act of 1934, a tax is imposed by the Parliament of Northern Ireland which is substantially the same in character as income tax.

In the first place, the Corporation contends that, while in form the contributions under Section 3 of the Act of 1934 are paid by the Council of a county or county borough to the Exchequer, and it is the Council that raise the amount of the contribution by means of the poor rate, the Council have no choice in the matter and are merely the hand by which the central authority imposes the levy on the ratepayers, which is, therefore, a tax imposed by the central authority on the ratepayers. In view of the opinion, formed by their Lordships on the second contention of the Corporation, it is unnecessary to decide this question, but their Lordships will assume that the first contention of the Corporation is correct.

It, therefore, remains to consider the second contention of the Corporation, namely, that the tax so imposed by the central authority on the ratepayer is "substantially the same in character" as income tax.

Counsel for the Corporation sought to establish this substantial similiarity in character by a detailed comparison of the provisions of the Income Tax Act, 1918, under Schedule A and in particular Schedule B, with the provisions of the Poor Relief (Ireland) Act, 1838, along with the fact under Section 187 (1), of the Income Tax Act, 1918, the value of all the tenement and rateable hereditaments for the purposes of Schedules A and B is ascertained primarily according to the valuation for poor rate purposes. But, in the opinion of their Lordships, it is the essential character of the particular tax charged that is to be regarded, and the nature of the machinery—often complicated—by which the tax is to be assessed is not of assistance except in so far as it may throw light on the general character of the tax. Such an examination as Counsel for the Corporation invited their Lordships to enter upon would tend to narrow the legislative powers of taxation of the Parliament of Northern Ireland almost to the vanishing point, whereas by Section 21 (1) of the Act of 1923, legislative powers are conferred in general terms, subject only to the specified exceptions.

In a familiar passage in *London County Council* v. *Attorney General*, Lord Macnaghten has described the character of income tax as follows:

"Income tax, if I may be pardoned for saying so, is a tax on income. It is not meant to be a tax on anything else. It is one tax, not a collection of taxes essentially distinct. There is no difference in kind between the duties of income tax assessed under Sch. D and those assessed under Sch. A or any of the other schedules of charge. One man has fixed property, another lives by his wits; each contributes to the tax if his income is above the prescribed limit. The standard of assessment varies according to the nature of the source from which taxable income is derived. That is all."

The purpose of the Income Tax Acts is to tax a person's total income from all sources; the method of assessing income derived by ownership or occupation of hereditaments is somewhat arbitrarily based on annual value and not on actual income but that does not alter the essential characteristic of income tax that it is a tax on income generally.

On the other hand, the poor rate is levied in respect of the occupation of hereditaments, irrespective of a person's income generally, and irrespective of whether the ratepayer is in fact deriving profits or gains from such occupation. A dwelling house is a burden, not a source of profit, for the occupier who pays rent for it. He is rated on the value of the burden, while he remains unrated in respect of his whole profits, be they from business or from investments. In their Lordships' opinion this marks the essential difference in character between income tax and rates, and it is unnecessary to consider other and less important differences between them.

Their Lordships are, therefore, of opinion, even assuming that under Section 3 of the Finance Act of 1934, a tax is imposed on the ratepayers by the central authority, that such tax is not substantially the same in character as income tax, and that the provisions of Section 3 are within the powers of the Parliament of Northern Ireland. Their Lordships will humbly advise His Majesty accordingly.

Order accordingly.

Solicitors: *Messrs. Dyon Bell & Co.*, for the Appellants.

Messrs. Linklater & Pains, for the Respondents.

[IN THE ALLAHABAD HIGH COURT.]

RATANCHAND LALLUMAL, *In re.*

BAJPAI and MULLA, JJ.

September 10, 1935.

INCOME TAX—ACCOUNTS ON CASH BASIS—PAYMENTS TOWARDS INTEREST—PAYMENTS ESCAPING ASSESSMENT OWING TO DEVICE OF ASSESSEE—ASSESSMENT AT LATER PERIOD WHEN DEVICE IS DISCOVERED—LEGALITY—HINDU UNDIVIDED FAMILY—PARTITION—PARTITION FOLLOWED BY AWARD—DATE OF PARTITION—REFERENCE—COMMISSIONER'S DUTY TO SUPPLY STATEMENT OF CASE TO ASSESSEE—STATEMENT OF CASE, WHETHER INCLUDES COMMISSIONER'S OPINION—ALLAHABAD HIGH COURT RULES, RULE 7—INDIAN INCOME TAX ACT (XI OF 1922), SECTIONS 3 AND 66.

The mere fact that a certain income has not suffered tax because of a device adopted by the assessee would not enable the department to assess the same in subsequent years when the device becomes apparent to the department. It is only when according to the particular system adopted by the assessee allocations are made not in the year when the amount is received but in later years that the income so allocated can be said to be income liable to be considered in the assessment year.

A Hindu undivided family advanced a loan of Rupees 2 lakhs in 1918. There was a partition in the family in 1921 and this debt fell to the share of the assessee. The debtor paid various sums of money to the assessee towards interest in the years 1923 to 1927. The assessee who kept his accounts on cash basis, entered these payments in his books; but he also made some cross entries relating to them to evade income tax. These payments were not shown in the return though the account books were produced and, as the income tax department also did not carefully scrutinise the accounts, these payments were not assessed to income tax. In 1930 the assessee realised Rupees two lakhs by selling a decree which he obtained in 1929 against the debtor for the loan advanced. In making the assessment for the year 1931-32 the income tax authorities added up all the receipts and expenditure in respect of the loan from 1923 to 1930 and treated the difference as income received for the assessment year 1931-32 and levied income tax on the same : Held, *on a reference by the Commissioner of Income Tax, that as the assessee's accounts were admittedly kept on the cash basis and there were no allocations by the assessee in 1930 the payments received by the assessee from the debtor during the years 1923-27 should not have been taken into account in making the assessment for 1931-32.*

Where there was a private partition amongst the members of a Hindu family in 1921 and certain arbitrators who were appointed by the parties to effect the partition delivered an award in 1925 which itself stated that the partition should take effect from 1921 and the award was made a rule of the Court in 1926 : Held, *that the partition of the family must be deemed to have been effected in 1921 and not in 1925 or 1926.*

The opinion of the Commissioner is different from his statement of the case and the Commissioner is not therefore bound under Rule 7 of the Rules framed by the Allahabad High Court under Section 66 of the Income Tax Act to give a copy of his opinion also to the assessee. The Rule is sufficiently complied with if he gives the statement of the facts of the case without his opinion.

Cases referred to:

COMMISSIONER OF INCOME TAX *v.* SIR KAMESHWAR SINGH [1933] (1 I.T.R. 94).

RAGHUNANDAN PRASAD SINGH *v.* COMMISSIONER OF INCOME TAX, BIHAR AND ORISSA (I.L.R. 9 Pat. 48).

RAGHUNANDAN PRASAD SINGH *v.* COMMISSIONER OF INCOME TAX, BIHAR AND ORISSA [1933] (1 I.T.R. 113).

Application under Section 66 (3) of the Income Tax Act. The facts are stated in full in the Judgment.

Gopi Nath Kunzru and *Krishna Murari Lal*, for the assessee.

K. Varma, for the Income Tax Department.

JUDGMENT.

The judgment of the Court was delivered by

MULLA, J.—By an order dated February 16, 1934, passed by a bench of this Court the Commissioner of Income Tax was directed under the provisions of section 66 (3) of the Indian Income Tax Act to state a case on certain questions, the Commissioner having refused to state the same on the application of the assessee under Section 66 (1). The questions formulated by this Court are:—

(1) Whether the payments made by M. K. Khanna from November 16, 1923, to September 9, 1927, were rightly taken into account in making the assessment for the year in question 1931-32?

(2) Whether in law the partition of the family was effected from the date of the decree or award, or from the year 1921 as held by the Assistant Commissioner of Income Tax?

(3) Whether Rs. 44,611-9-9 realised from M. K. Khanna in Sambat 1980-81 is liable to income tax as the income or profit of the assessee, or is this sum exempt from income tax under Section 14 of the Income tax Act?

The case has now been stated by the Commissioner which is the subject of Miscellaneous Reference No. 456 of 1933. Allied with this Reference is another Miscellaneous Reference No. 457 of 1933 in which under similar circumstances the question that arises for determination is as follows:—

(4) Whether on the facts found the assessee has concealed the particulars of his income or has deliberately furnished inaccurate particulars of his income and is, therefore, liable to penalty under Section 28 of the Income Tax Act?

In order to answer the questions satisfactorily it will be necessary to state a few facts. The Reference has arisen out of the assessment made in the year 1931-32. Under Section 3 of the Act the assessment shall be in respect of all income, profits and gains of the previous year. The previous year in the case of the present assessee, according to the system of accounts maintained by him, would be the year beginning from Kuar Sambat 1986 to Kuar Sambat 1987. The assessee is a Hindu undivided family of Azamgarh which goes by the name of Messrs. Ratan Chand Lallu Mal of Azamgarh and Rai Bahadur Mukand Lal is the head of the family. As a matter of fact this family came into existence as a result of the disruption of a bigger Hindu undivided family known as Messrs. Sital Prasad Kharag Prasad of Calcutta and the head of this bigger family was the late Raja Sir Moti Chand of Benares, and one of the questions that we shall have to decide is as to when there was a partition of or separation in the bigger Hindu undivided family. The assessee began to be taxed from the year 1925-26 on the income of the previous year which ran from Kuar 1980 to Kuar 1981. The first and the most important question is whether the payments made by M.K. Khanna from November 16, 1923, to September 9, 1927, were rightly taken into account in making the assessment for the year in question 1931-32. It is clear that the assessment year being 1931-32 the income of the previous year 1930-31 ought to be ordinarily taken into consideration and the payments made or income received from November 1923 to September 1927 would be beyond the scope of assessment, but it is the case for the department that under the peculiar circumstances of this case the above income made in those years can also be taken into consideration.

It appears that on March 31, 1918, a loan of Rs. 2,00,000 was advanced by the late Sir Moti Chand to Mr. Maharaj Kishore Khanna. The amount due under this loan fell to the share of Ratan Chand Lallu Mal after partition in the bigger family of Sital Prasad Kharag Prasad. Payments were made by Mr. Khanna from time to time to Rai Bahadur Mukand Lal.

The first payment for the purpose of this case was made in November 1923 and the sum so paid was Rs. 10,000. In the assessment year for 1925-26 when this payment along with certain other payments made in the previous year 1923-24 ought to have been taken into consideration, the assessee did not show them in his return nor did the department assess any tax on those payments. It is, however, quite clear that as much as Rs. 44,611-9-9

was received by the assessee. The appellate order of the Assistant Commissioner dated March 28, 1933 shows that in the books of the assessee the entries are :—

On Katik Sudi Asthami Sambat 1980 as interest	10,000	0	0
On Katik Sudi 11 Sambat 1980 as interest	20,000	0	0
On Pus Badi 13 Sambat 1980 as interest	6,532	11	3
On Bhadon Badi 1 Sambat 1981 cheque on Benares Bank—the word interest not noted	8,000	0	0
On Bhadon Badi 13 Sambat 1981 corresponding to August 28, 1924, cheque—the word interest not noted	78	14	6
	44,611	9	9

In connection with the first three items the words " as interest" are noted definitely in the assessee's account books. These items were then transferred from the account of Mr. Khanna and the entries that were subsequently made in a separate account were to the effect that Rs. 40,150-7-3 were credited to the personal account of Rai Bahadur Makund Lal and Rs. 4,461-2-6 were credited to the Dharmada account. These entries were made on Augst 28, 1924 and this date corresponds with the last entry of Rs. 78-14-6 to which reference has already been made. By reason of the fact that the assessee did not show this sum as his income in the return furnished by him and the department also failed to scrutinise the account books carefully the whole of this income escaped assessment in the assessment year 1925-26.

In the assessment year 1926-27 the assessee was taxed on certain income which undoubtedly included the sum of Rs. 16,139-8-0 received from Mr. Khanna on Pus Sudi 7, 1981 and October 2, 1925. The learned Assistant Commissioner says, " that the appellant declared this income for the assessment of the year 1926-27 and it was actually included in the assessment of that year." We now come to the assessment year 1927-28 when the income for the previous year 1925-26 or Kuar Sambat 1982 to Kuar Sambat 1983 would be taken into consideration. In this year also the assessee received a sum of Rs. 16,521-8 6, but once again he did not show it in his return and the Revenue authorities also failed to detect it. It is not quite clear either from the statement of the case or from the orders of the Income Tax Officer and the Assistant Commissioner whether this sum was in the first instance credited

in the account of Mr. Khanna as interest, although there is a stray passage in the judgment of the Assistant Commissioner wherein he says that "this interest was not credited to the interest account." Now there are certain entries which require mention. We have stated above that on August 28, 1924 the sum of Rs. 44,611-9-9 was credited to the personal account of the assessee in the sum of Rs. 40,157-7-3 and to the Dharmada account in the sum of Rs. 4,461-2-6, but in the year 1982-83 the account books show that a sum of Rs. 52,611 which included the above sum of Rs. 44,000 odd and a sum of Rs. 8,000 received on Pus Sudi 7, 1981, was at first credited to the interest account, then debited to the interest account and finally credited to the personal account of Mr. Khanna. Whether these entries escaped the attention of the Revenue authorities is not quite clear from the statement of the case, but from a passage in the judgment of the Income Tax Officer dated April 23, 1932 it would be reasonable to infer that the revenue authorities did come to know of these entries, for it is stated in the order just referred to while considering the entry of the sum of Rs. 52,611 that "it is not known how the cross entries of the interest account were explained away before Mr. S. M. Husain". As to the sum of Rs. 16,521-8-6 the entries are to the effect that this sum was credited to the account of the appellant's son Indu Bhushan and from that account it was subsequently transferred to the account of Rai Bahadur Makund Lal. In the assessment year 1928-1929 which was for the income of the previous year 1926-27 corresponding to Kuar Sambat 1983-84 once again the assessee did not show any income from Mr. Maharaj Kishore Khanna. In the assessment year 1929-30 which related to the income of the previous year 1927-28 corresponding to Kuar Sambat 1984 to Kuar Sambat 1985 the assessee did not file any return but he produced certain accounts which, however, did not show any income received from Mr. Khanna and the assessment was made under Section 23 (4) according to the best of the Income Tax Officer's judgment. In the assessment year 1930-31 which related to the income of the previous year 1928-29 corresponding to Kuar Sambat 1985 to Kuar Sambat 1986 the assessee did not show any income from Mr. Khanna and the Income-tax Officer assessed him on a certain income which was arrived at after making certain calculations.

It is not of any great importance to find out whether any income was received by the assessee from Mr. Khanna after September 9, 1927 till we come to the assessment year 1931-32

which relates to the income received in the previous year 1929-30 corresponding to Kuar 1986 to Kuar 1987, because the income received after September 9,1927 is not to be considered in connection with the answer to question No. (1). It is also not necessary to state the circumstances under which the Income Tax Officer, when dealing with the assessment year 1931-32, came to realise that certain income received by the assessee from Mr. Khanna in the years 1923 to 1927 escaped assessment. These circumstances have been stated in detail in the case prepared by the Commissioner and neither party has taken any objection to that statement. From the order of the Income Tax Officer it appears that what he did was to add up the receipts from Katik Sudi 8, Sambat 1980 corresponding to November 1923 to August 11, 1930 which give the figure of Rs. 2,95,997-6-0. He then put down certain figures on the expenditure side and arrived at the total of Rs. 2,32,208. On the expenditure side he showed the amount received in consequence of the partition as principal at the figure Rs. 1,98,580 and a sum of Rs. 16,139-8-0, the amount which was actually assessed to income-tax in the assessment year 1926-27. He then considered the difference between the two totals amounting to Rs. 63,789-6-0 as income received in the assessment year 1931-32 and levied a tax on the same.

The contention of the assessee is that the method adopted by the Income Tax Officer and confirmed by the Assistant Commissioner is objectionable and not warranted by law. It is said that under Section 3 all that could be taxed was the income received during the previous year, namely 1929-30 corresponding to the period Kuar 1986 to Kuar 1987, and if that income alone is taken into consideration we can take into account only the last three figures on the receipt side mentioned at page 14 of the printed record and a deduction will have to be made therefrom or the return of the capital which would probably be represented by the first and the third item out of those three figures. It appears that Rai Bahadur Makund Lal brought a suit on the basis of the mortgage of March 31, 1918 and obtained a decree for Rs. 2,58,999 on November 21, 1929. He subsequently sold the same on April 25, 1930 to one Rai Krishna Das of Benares for Rs. 2,00,000 and this amount was received by the assessee in two sums, one on Phagun Sudi 11, 1986 and the other on August 11, 1930. It would therefore appear that if a sum of Rs. 2,00,000 representing the capital is deducted from the income received in the year 1929-30 all that the assessee received from Mr. Maharaj Kishore Khanna as

interest amounted to about Rs. 3,000. The Income Tax Officer is of the opinion that with the exception of Rs. 16,139-8-0 the various sums that were received by the assessee from time to time during the period from November 16, 1923 to September 9, 1927 were not treated by him as interest and it comes with an ill grace from his mouth that these items are not assessable to income-tax in the year in question because they were received prior to the previous year. Relying upon the Patna case of *Raja Raghunandan Prasad Singh* v. *The Commissioner of Income-tax, Bihar and Orissa* the Income Tax Officer arrived at the conclusion that the income by way of interest received from M.K. Khanna was assessable in the year in question even though it had been received prior to the previous year—excluding of course the amount that had already been taxed. The learned Assistant Commissioner says that the natural inference is that the assessee treated the income of Rs. 44,611-9-9 as a part payment of the loan and that he did not treat the sum of Rs. 16,521-8-6 as income of the year 1926-27 on the assumption that the loan itself was doubtful and consequently when the loan was realised in full, that is, in the year 1930-31, the interest so derived from it became liable to be taxed. While giving his opinion the learned Commissioner of Income tax also refers to the Privy Council case of *Commissioner of Income Tax, Bihar and Orissa* v. *Kameshwar Singh of Darbhanga*. It might be mentioned here that the decision of the Patna High Court in *Raghunandan Prasad Singh's case*, was affirmed in appeal by the Privy Council and the report of the decision of their Lordships of the Privy Council is to be found in 1933 A.L.J. 564 (1933 I.T.R. 113).

The question that we have got to decide is whether the decision to which reference has been made apply to the facts of the present case. We have made it clear that in spite of certain cross-entries and reverse entries the sum of Rs. 44,000 odd could, on a little investigation, have been discovered as pertaining to the loan advanced to Khanna and as having been received as interest. Indeed the learned Assistant Commissioner definitely says that the income of Rs. 44,611-9-9 in dispute was received by the assessee on account of interest in the previous year Kuar 1980-81. The position taken by the department is that the payments made by Khanna from November 16, 1923 to September 9, 1927 were kept in suspense and the receipts were treated as open receipts on the ground that the assessee was either not clear as to his position in connection with the partition that was being effected between himself and the bigger Hindu undivided family or that he

was not hopeful of the loan being realised from M.K. Khanna and he was waiting to see how the loan would finally be. It might be mentioned that these two grounds were stated by certain servants of the assessee when the assessment for the year 1931-32 was being made and not at the time when the income was actually received. The facts, however, speak for themselves and it is not possible to attach any importance to such statements when they were made in order to explain away certain concealments made in previous years. There seems to be no room for doubt as to the real nature of the payments made by Mr. Khanna. We need not repeat what we have already said in an earlier portion of our judgment that the entries in the books show that most of these sums that were entered as interest in the books of the assessee were shown in the account of Mr. Khanna and were subsequently by means of cross entries or reverse entries transferred to the account of Rai Bahadur Makund Lal. This to our mind therefore is not a case where it can be said that the amounts were kept in suspense. The whole object of the entries was to evade the legitimate tax. The Income tax officer says that "in the personal account of Maharaj Kishore Khanna several cross entries have been made and the real income from interest has been obscured." The learned Commissioner in his statement says "in the personal account of Mr. Khanna several cross entries had been made with a view to obscure the real income from interest." If, therefore, after a little investigation, the Revenue authorities at the present moment are in a position to know the real object of entries it is their own fault if they could not detect this object at an earlier stage. It is nobody's case that the various account books which have enabled the authorities to come to this conclusion were not available to them in the earlier years. The statement shows that account books were summoned from the assessee and were produced.

We shall now consider whether there is anything in law to justify the procedure which the department has adopted in the present case. At one stage it was boldly argued by the counsel on behalf of the department that it was open to the Revenue authorities even if income was received in previous years to tax it in the assessment year when the transaction was finally closed. This is in the teeth of the provisions of Section 3 of the Indian Income Tax Act. The only question is whether the transaction having been closed in the assessment year it is possible for the authorities to take into consideration the receipts not only of the previous year

but also those of years anterior to the previous year on the ground that they were in the nature of open receipts In *Raghunandan Prasad Singh's* case all that was held by their Lordships of the Patna High Court was that where a person advances money on a mortgage and subsequently gets the interest added to the principal and takes a fresh mortgage for the consolidated amount but does not show the added interest separately as interest realised in his books of account of that year in the interest account or in his personal account, the inference is that the original bond is not extinguished from the point of view of the Income Tax administration since nothing is received by him as income, profit or gain in that year. That is obviously correct because unless the accounts of the assessee are kept on the mercantile basis the interest which has not been actually received has only gone to swell the amount of the next transaction and it is not possible to say that the assessee made any profit or gain in the year when the fresh mortgage was drawn up. In this very case it also appeared that on the fresh mortgage the mortgagee brought a suit and after having obtained a decree purchased the property in execution of the decree. It was held that the mortgagee assessee could not be deemed to have received any income or its equivalent as long as the sale had not been confirmed. It was said that till then the position of the decree holder was not secure and it was open to the assessee to say that till then he did not propose to deal with the money as in any way belonging to him. We are in perfect agreement with this view and further we are bound by this view inasmuch as it was confirmed by their Lordships of the Privy Council. But in the present case unless it can be argued that it is open to a money lender to treat every income which he receives from his debtor by way of interest as an item in suspense till the final account is closed the procedure adopted by the department cannot be countenanced nor do we think that it would be in the interest of the department to allow money lenders to treat all income received from their debtors in suspense till the account is finally closed either by payments made out of Court or when the transaction has been made the subject of a suit and money realised in execution of a decree. In the case of *Commissioner of Taxes* v. *The Meblourne Trust Ltd.*, Lord Dunedin observes :

"As regards the question of when a profit is earned their Lordships' view is that a profit can be said to be earned when it is dealt with as a profit. In ordinary cases this synchronizes with the realisation of the sums which swell the assets of the person or

company, and which entering the account go to bring out the balance which is deemed profit."

In the particular facts of the case before their Lordships where the question was as to whether a certain company which had come into existence for the purpose of realising outstandings due to certain other companies which had gone into liquidation was liable to income tax on the surplus realized as profits it was held that the new company was entitled to keep certain sums in suspense. The facts of that case were entirely different, but even there the principle was affirmed that ordinarily profit synchronizes with the realisation of the sums which swell the assets of the assessee.

We have left for consideration the last case of *Commissioner of Income Tax, Bihar and Orissa* v. *Kameshwar Singh of Darbhanga.* The facts of this case were that there was no well recognised method in which the account books of the assessee were kept. Their Lordships emphasise that "the questions which have arisen in the case are in large measure due to the assessee's method or want of method in recording his money-lending transactions". The system which he kept was a hybrid system, in the sense that he maintained a deposit register in which payments made by debtors were ordinarily first of all recorded but without any allocation between principal and interest and subsequently if and when the allocation was made an entry in respect of the interest portion of these payments was made in the interest ledger as well as in the interest account of the general ledger but, this allocation was not necessarily made in the year in which the money was actually paid to the assessee. The deposit register was not made available to the Revenue authorities and all that they had before them was the interest register. In the assessment year in question for the first time the deposit register came before the income tax authorities and on this occasion the Income Tax Officer made his computation by taking first all the sums allocated to interest and entered in the interest register for that year, irrespective of the years in which these sums had actually been received by the assessee; he then resorted to the deposit register, noted the sums there shown actually received in that year by the assessee but from which no allocations to interest had been carried to the interest register, made his own calculation of the proportions of interest comprised in such sums and added the result to the sum of the entries in the interest, for that year,

It was pointed out that owing to the system on which the interest register was kept the assessee was in each year assessed not on the total of the sums actually received by him as interest during the preceding year but on such sums as the assessee chose during that previous year to allocate to interest and carry to his interest register out of payments received by him in that and former years. In this case it is obvious that the assessee cannot complain if he is treated as not having received any payment of interest in years in which he made no appropriations to interest out of sums received by him in these years and neither disclosed such receipts to the Revenue authorities nor made any return of any part of them as income.

The Income Tax Officer says that it comes with ill grace from the assessee's mouth that the sum of Rs. 52,611 was not assessable to income-tax in the year in question because it had been received prior to the previous year, but this statement is not quite correct inasmuch as the mere fact that a certain income has not suffered tax because of a device adopted by the assessee would not enable the department to assess the same in subsequent years when the device becomes apparent to the department. It is only when according to a particular system adopted by the assessee allocations are made not in the year when the amount is received but in later years that the income so allocated can be said to be the income liable to be considered in the assessment year. From what we have stated above it is clear that the allocations were made by the assessee himself and all that the income tax officer did was to make certain calculations from the deposit register as well which became available to him when he was making the assessment.

In the present case it is common ground that no fresh allocations were made by the assessee either in the assessment year or in the previous year and as the learned Commissioner says: "the accounts had always been cast on what was known as the cash basis". Their Lordships of the Privy Council observe at the bottom of page 631 of the Reports, (1933 A.L.J.):

" When an assessee keeps his books on a cash basis disclosed to the Revenue authorities and the officer accepts that basis it is clear that the calculation must be based on actual receipts in the year of computation ".

In the case of this assessee therefore the calculation must be based on actual receipts in the year of computation. The learned

Commissioner was conscious of this difficulty and therefore he observed:

"It is clear that the question resolves into one of the allocation of the amount of Rs. 2,03,397-3-0 admittedly received in the accounting year, but if this figure which was received in the accounting year be alone taken into consideration the figure of Rs. 63,779 on which the assessee has been taxed cannot possibly be evolved. A reference to page 14 shows that the figure of Rs. 63,779, was obtained by taking sums on the receipt side and on the expenditure side for a number of previous years".

We are therefore of the opinion that the payments made by Maharaj Kishore Khanna from November 16, 1923 to September 9, 1927 should not be taken into account in making the assessment for the year in question, 1931-32.

We now propose to consider the second question which relates to the time when the bigger family can be said to have separated. From what has been stated before us it is clear that there was a private partition in Sambat 1978 corresponding to October 1921 between Raja Sir Moti Chand, Babu Shiva Prasad Gupta, Babu Karakh Chand, Rai Bahadur Makund Lal and other members of the bigger family. The assessee had no separate entity before 1921. He had no business and no income of his own, but after that time he has been doing money-lending business, is in enjoyment of income from dividends and interest on securities and has a 9 annas share in a Gorakhpur firm. From the year 1925 he has been regularly assessed to income tax. The contention of the assessee that the separation of the family should be deemed to have come into existence on November 30, 1925 when certain arbitrators who had been appointed by the members of the family to effect a partition delivered their award or when the award was made a rule of Court on February 26, 1926 cannot be upheld inasmuch as all the circumstances point to the fact that the disruption of the family took place at an earlier date, namely, 1921 when the parties not only declared their intention to separate but started separate business of their own. As a matter of fact in the case of *Shiva Prasad Gupta* v. *The Commissioner of Income Tax, United Provinces*, it was held that Mr. Shiva Prasad Gupta, another member of the same bigger family, was separate from the time of the private partition. It is conceded by Mr. Kunzru on behalf of the assessee that the award itself says that the partition will take effect from Sambat 1978, that is, the year 1921

and the award and the decree say the same. In this state of affairs it is clear that the partition or separation of the family was effected from the year 1921 as held by the Assistant Commissioner of Income Tax.

Coming now to the third question we are of the opinion that the income of Rs. 44,611-9-9 realised from Mr. Khanna in Sambat 1980 to 1981 cannot be exempted from income-tax under Section 14 of the Income Tax Act. That provision says that the tax shall not be payable by an assessee in respect of any sum which he receives as a member of a Hindu undivided family. The family did not remain a Hindu undivided family in the year 1980-81, the division having taken place in Sambat 1978 and the above mentioned sum could not be said to have been received by Rai Bahadur Makund Lal as a member of a Hindu undivided family. It is common ground that when we are speaking of a Hindu undivided family we are speaking of the bigger family of Sital Prasad Kharakh Prasad and not the smaller family of Ratan Chand Lallu Mal.

Our decision therefore is that question No. (1) should be answered in the negative, that the answer to question No. (2) is that the partition of the family was effected from the year 1921 as held by the Assistant Commissioner of Income Tax and the answer to question No. (3) is that the sum of Rs. 44,611-9-9 realised from Maharaj Kishore Khanna in Sambat 1980-81 is liable to income tax as the income or profit of the assessee and is not exempt from income-tax under Section 14 of the Indian Income Tax Act. We are of the opinion that for the present assessment it cannot be taxed by reason of our answer to question No. (1).

We might now notice a preliminary objection that was advanced by Mr. Kunzru before the hearing of this case commenced. It was said that the learned Commissioner of Income-tax has not complied with Rule 7 of the Rules framed by this Court under Section 66 of the Indian Income-tax Act. That rule says that the Commissioner of Income-tax having stated a draft case shall submit the same to the assessee or his counsel etc., etc. It is conceded that the case from page 1 to about 10 lines of page 9 of our printed record was submitted to the assessee. The opinion of the Commissioner on the various questions as given in pages 9 to 11 was not supplied and it is said that that too is a part of the draft case and should have been supplied to the assessee. We are of the opinion that there is no force in this contention inasmuch as a reference to Section 66 of the Indian Income-tax Act clearly shows that the opinion of the Commissioner is something different from the state-

ment of the case. In sub-Clause (1) it is provided that the Commissioner shall draw up a statement of the case and refer it with his own opinion thereon to the High Court and a similar provision exists in Sub-clause (2). This makes it quite clear that the opinion of the Commissioner is different from the statement of the case, and there was a complete compliance by the Commissioner with Rule 7.

A copy of our judgment under the seal of the Court and the signature of the Registrar will be sent to the Commissioner of Income-tax. We tax the fee of the counsel for the department at Rs. 200, and he is given a month's time to file the necessary certificate. We award no costs to the assessee against the department because we are of the opinion that his conduct in trying to evade the income-tax for a number of years is most reprehensible.

Reference answered accordingly.

[IN THE LAHORE HIGH COURT.]

MIAN CHANNU FACTORIES UNION

v.

COMMISSIONER OF INCOME-TAX, PUNJAB.

SIR JAMES ADDISON and ABDUL RASHID, JJ.

February 10, 1936.

ASSOCIATIONS—PARTNERSHIP BETWEEN FIRMS OWNING GINNING FACTORIES—WHETHER CAN BE REGISTERED AS FIRM—FIRM, DEFINITION OF—PROPER MODE OF ASSESSMENT—INTEREST PAID TO PARTNERS ON MONEY INVESTED FOR PURCHASING GOODS—WHETHER ALLOWABLE AS INTEREST ON MONEY BORROWED—INDIAN INCOME-TAX ACT (XI OF 1922), SECTIONS 3, 26-A AND 10 (2) (ii).

Two firms and a Hindu undivided family each of which owned a ginning factory entered into a partnership. They were to own 70, 60 and 75 shares respectively in the partnership. Goods were to be purchased by each factory with its own capital, but all goods purchased by the partnership were to be sent to the three factories in proportion to their respective shares and each factory was to charge Rs. 10 per bale for ginning and Rs. 10 per cent. per annum interest on the capital invested by it. The factory ginning was

to keep Rs. 5·8 per bale and to pay Rs. 4-8 to the partnership. At the end of the year the profits made by the partnership were to be divided between the three constituents in accordance with their respective shares. On a reference by the Commissioner: Held, (*i*) *that the union was a trading concern and as such liable to assessment on the profits*;

(*ii*) *that since a firm is only a group of individuals and one firm cannot be a member of another firm, the union was not a 'firm' within the meaning of the Income-tax Act, but it was liable to be assessed as an 'association of individuals'*;

(*iii*) *in any event the union could not be registered as a firm as the shares of the individuals composing the firms were not mentioned in the deed of partnership*; *and*

(*iv*) *the money invested by the different partners from purchase of goods was not capital borrowed for the business within Section 10 (2) (iii) of the Income-tax Act.*

Case referred to:

PANNAJI DEVICHAND *v.* KAPURCHAND [1927] (50 M. 175; A.I.R. 1927 Mad. 123; 99 I.C. 640) affirmed by the Privy Council in 34 C.W.N. 1107; A.I.R. 1930 P.C. 800; 59 M.L.J. 435.

Case stated by Commissioner of Income-tax, Punjab & N. W. F. P., under Section 66 (2) of the Indian Income-tax Act (Ref. No. 55 of 1935).

The necessary facts appear in the Judgment.

M. L. Sethi and *J. G. Sethi*, for the assessees.

J. N. Aggarwal, and *S. M. Sikri*, for the Commissioner of Income-tax, Punjab.

JUDGMENT.

SIR JAMES ADDISON, J.—This is a reference under Section 66 (2) of the Indian Income-tax Act. The Commissioner of Income-tax, Punjab, has formulated the following questions of law for the opinion of this Court:—

(1) Whether on the facts of the case, the assessees were chargeable to tax under Section 3 of the Income-tax Act?

(2) Whether the assessees were to be dealt with as a "firm" or as an "association of individuals"?

(3) Whether registration under Section 26-A could be granted or not?

(4) Whether, in the circumstances of the case, interest paid to partners was an allowable deduction under Section 10 (2) (*iii*)?

The Mian Channu Factories Union (hereafter called the assessees), were assessed for the year 1933-34 on an income of Rs. 39,969 in the status of an "association of individuals"

This union was constituted by means of a deed of partnership dated 13th September, 1931. There were three partners according to the partnership deed, namely, the firm of Dhanpat Mal-Diwan Chand, the firm of Ujjal Singh-Ajaib Singh and the Hindu undivided family of Dhanpat Mal-Bhagwan Das, described as the first, the second and the third party, and owning 70, 60 and 75 shares in the partnership respectively. It was provided in the deed that all the goods purchased by the partnership shall be sent to all the three factories for ginning in proportion to their respective shares and that each factory shall charge Rs. 10 per bale for ginning. The factory ginning was to keep Rs. 5-8 per bale and pay Rs. 4-8 to the partnership. At the end of the year the profi made by the partnership was to be divided between the partners in accordance with their respective shares. Any amount remaining unrealised from a purchaser or an *Arthi* was to be borne by the partnership. The partnership was to pay the employees and the ginning charges were to be debited to each factory after the whole lot was pressed. In view of the above-mentioned provisions of the deed of partnership it is clear that the Union was a trading concern and as such liable to assessment on its profits. In the case reported as I.L.R. 50 Mad. 175, four unregistered firms entered into partnership to purchase certain goods, to sell them at different times and divide the profits and it appeared that the total number of members of all the firms together came to twenty-two, but the partnership was not registered under the Indian Companies Act. On a suit instituted by three of the firms against the fourth for dissolution of partnership and taking of partnership accounts, it was held that the transaction was a business within Section 4, Clause 2, of the Indian Companies Act, and not a single venture falling outside the section. It was further held that for purposes of registration required by Section 4, Clause 2, of the Act, each of the unregistered firms cannot be regarded as a single legal entity; that "persons" under Section 4, Clause 2, denotes individuals and does not include bodies of individuals. This decision was affirmed by their Lordships of the Privy Council (34 C.W.N. 1107).

It is well-settled that a firm is a mere group of individuals, and that a firm as such cannot legally be partner in another firm. In the present case the Mian Channu Factories Union purports to

consist of two firms and one Hindu undivided family. The shares of the members of the firm Dhanpat Mal-Bhagwan Das and those of Ujjal Singh-Ajaib Singh *inter se* are not mentioned in this deed of partnership. While this partnership is undoubtedly a trading concern, it does not appear to us to fall within the definition of the word "firm" as given in the Income Tax Act. It is more appropriate to regard it as "Other Association of Individuals".

In view of our finding that the union is not a firm, the question of registration really does not arise. In any case, even if the Union is held to be a firm, it cannot be registered as the individual shares of the different members of the firm constituting the partnership are not mentioned in the deed.

With regard to interest it is provided in the deed af partnership that each factory shall invest its own capital for the purchase and sale of goods and shall get interest at the rate of Rs. 10. *per cent. per mensem.* The money thus used by the different partners cannot be considered to be capital borrowed for the purposes of the business within the meaning of Section 10 (2) (iii).

For the reasons given above, we answer the first question in the affirmative. With respect to the second question we hold that assessees must be regarded as an "association of individuals". The third and the fourth questions are answered in the negative. The assessees shall pay the costs of the Commissioner in this Court.

[IN THE LAHORE HIGH COURT.]

MELAMAL-SHIB DAYAL

v.

COMMISSIONER OF INCOME TAX, PUNJAB.

SIR JAMES ADDISON and ABDUL RASHID, JJ.

February 10, 1936.

INCOME TAX—ACCOUNTING YEAR—NEED NOT NECESSARILY BE FINANCIAL YEAR—SAMBAT YEAR—INDIAN INCOME TAX ACT (XI OF 1922), SECTION 13.

The provision contained in Section 13 of the Indian Income Tax Act to the effect that income, profits and gains shall be computed

in accordance with the method of accounting regularly employed by the assessee does not imply that the assessee must necessarily adopt the financial year as the accounting period or must adopt a method which would avoid two dates of 31st March falling within one accounting period.

Civil Miscellaneous Petition (No. 620 of 1935) under Section 66 (3) of the Indian Income-tax Act, 1922, for a mandamus requiring the Commissioner of Income-tax, Punjab, to state a case.

Kirpa Ram Bajaj, for the petitioner.

J. N. Aggarwal and *S. M. Sikri*, for the Commissioner of Income-tax.

ABDUL RASHID, J.—This is an application under Section 66 (3), Indian Income-tax Act, for a mandamus to compel the Commissioner of Income-tax, Punjab, to state the case of the firm Mela Mal Shib Dayal and refer the points of law arising therein to the court. The following questions of law have been formulated on behalf of the assessees: (1) whether the sum of Rs. 2,062 on account of loss of the Ferozepore excise branch, and Rs. 4,663 of Mahalpur, Hariana and Moga, which follow the financial year as their accounting periods (1st April, 1930 to 31st March, 1931) should not have been allowed to the assessees in the assessment relating to the year 1932-33 which follows the accounting period *Chet Sudi* 1 to *Chet Badi* 15 which corresponds to 20th March, 1931 to 5th April, 1932, for the year under assessment; (2) when a method of accounting is regularly employed by an assessee and the same is accepted by the Income-tax Officer from year to year, is an Income-tax Officer legally justified in departing from that practice in any subsequent year?

It appears that the head office of the assessees' firm is at Hoshiarpur and they also carry on business at Ferozepore, Mahalpur, Hariana and Moga. The accounting period of the head office is the *Sambat* year from *Chet Sudi* 1 to *Chet Badi* 15. The length of the *Sambat* year is not constant, and sometimes it extends over two dates of 31st March, and sometimes it does not include even a single date of the 31st March. The accounting period of the branch offices which mainly deal with excise contracts is from the 1st of April to the 31st of March. That is the ordinary financial year. According to the assessees there was a loss at the Ferozepore excise branch amounting to Rs. 2,062 and at Mahalpur, Hariana and Moga branches amounting to Rs. 4,663 during the accounting period 1st

April, 1930 to 31st March, 1931. The acccounting period of the head office for the assessment year, 20th March, 1931 to 15th April, 1931, happened to correspond to the period from "30th March, 1930 to 19th March, 1931." As the accounting period of the head office ended before the accounting period of the branch offices came to an end, the losses of the branch offices during 1930-31 were not shown in the head office accounts dealing with the accounting period "30th March, 1930 to 19th March, 1931." In the assessment for the year 1932-33 the losses referred to above were sought to be claimed as they could not have been claimed in the previous year, as the accounting period of the head office ended before the accounting period of the branch offices had come to an end.

The learned Commissioner refused to state the case to this Court on the ground that the method of accounting resorted to by the assessees could not be regarded "as a regular method of accounting" under Section 13 of the Act. On the other hand it was claimed on behalf of the assessees that this "method of accounting" had been employed by the assessees for a number of years and the income-tax authorities had raised no objection thereto. We are of the opinion that the provision of Section 13, Income-tax Act, to the effect that income, profits or gains shall be computed in accordance with the method of accounting regularly employed by the assessees do not imply that the assessees must necessarily adopt the financial year as the accounting period or must adopt a method which would avoid two dates of 31st March falling within one accounting period. For the reasons given above, we direct the Commissioner of Income-tax, Punjab, to state the case of the petitioner and refer it to this Court. We formulate the following question of law: "Whether in the circumstances mentioned above the losses of the branches ought to have been allowed in the assessment year 1932-33 of the Head Office." The respondent will pay the costs of the petitioner.

Mandamus granted.

[IN THE RANGOON HIGH COURT].

COMMISSIONER OF INCOME TAX, BURMA

v.

DEY BROTHERS.

SIR ARTHUR PAGE, C. J., MYA BU, J., and BA U, J.

March 8, 1936.

RE-ASSESSMENT—SCOPE OF SECTION 34—RE-ASSESSMENT OF INCOME WHICH HAS ONCE BEEN ASSESSED—RE-ASSESSMENT ON SURMISES AND HYPOTHESES WITHOUT FOUNDATION—ILLEGALITY—BURDEN OF PROOF—INDIAN INCOME TAX ACT (XI OF 1922), SECTION 34.

Section 34 of the Indian Income Tax Act is applicable to cases in which either no assessment at all has been made upon the person who received the income, profits or gains liable to assessment, or where assessment has been made in the course of the year some portion of the income, profits or gains of such assessee for some reason or other has not been included in the order of assessment; such income is income which has 'escaped assessment' in the year and falls within the ambit of Section 34 of the Act. But income in respect of which a final and conclusive assessment has been made cannot be subjected to a revised assessment except when the assessment has been fixed at too low a rate.

The income of the assessee for the year 1931-32 was assessed at Rs. 8,267 after a scrutiny of his account books and income tax was levied accordingly. Thereafter as a result of a search upon the assessee's premises certain documents came into the possession of the income tax authorities and proceedings under Section 34 were started. The figures for later years, namely, for the years 1932-1933 and 1933-34 showed a larger profit on a smaller turnover and the Income Tax Officer estimated that 30 per cent. of the figure for sales in 1930-31 must have represented the gross profits and he re-assessed the income of the assessee for 1931-1932 upon that footing at Rs. 59,130.

Held, *that the assessment under Section 34 was based not upon facts but upon surmises and hypotheses for which there was no sound foundation; there were no materials from which the Income Tax Officer could have found that in the accounting year there were profits from the business which had escaped assessment and the revised assessment was therefore illegal.*

The animadversions passed by the Bombay High Court upon U Lu Nyo's Case *are not justified.*

Under Section 34 if the income tax authorities have not misdirected themselves in law and there were materials before the Income Tax Officers upon which they could find that income, profits and gains had in fact escaped assessment the Court will not interfere or disturb the finding of fact at which the income tax authorities have arrived. It cannot be broadly laid down that under Section 34 the onus is upon the income tax authorities to satisfy the Court upon the facts that income, profits and gains had escaped assessment so as to give the assessee a right of appeal on facts in the case of every assessment under Section 34.

COMMISSIONER OF INCOME TAX, BOMBAY *v.* G. V. MANOHAR [1935] (I.L.R. 59 Bom. 656; 158 I.C. 757; 1935 I.T.R. 372) *dissented from.*

COMMISSIONER OF INCOME TAX, BURMA *v.* U LU NYO [1933] (I. L. R. 12 Rang. 118; 146 I. C. 300; 1933 I. T. R. 373) *followed.*

Cases referred to:

ANGLO PERSIAN OIL CO. (INDIA), LTD., *In re* [1933] 60 Cal. 840; 34 C.W.N. 430; A.I.R. 1933 Cal. 777; 1933 I.T.R. 129).

BURN & CO., *In re* [1934] (61 Cal. 132; 38 C.W.N. 204; 150 I. C. 404; A.I.R. 1934 Cal. 515; 1934 I.T.R. 30).

COMMISSIONER OF INCOME TAX, BOMBAY *v.* G. V. MANOHAR [1935] (59 Bom. 626; 37 Bom. L. R. 697; 158 I. C. 757; A.I.R. 1935 Bom. 410; 1935 I.T.R. 372; 8 I.T.C. 273).

COMMISSIONER OF INCOME TAX, BURMA *v.* N. N. BURJORJEE [1931] (9 Rang. 161; 131 I.C. 507; 1931 Rang. 101; 3 I.T.C. 270).

COMMISSIONER OF INCOME TAX, BURMA *v.* T. S. T. S CHETTIAR FIRM [1931] 9 Rang. 28; 132 I.C. 559; A. I. R. 1931 Rang. 333).

COMMISSIONER OF INCOME TAX, BURMA *v.* U LU NYO [1933] (I.L.R. 12 Rang. 118; 146 I.C. 300; A.I.R. 1933 Rang. 350; 1933 I.T.R. 373).

COMMISSIONER OF INCOME TAX, MADRAS *v.* R. SUNDARESA AIYAR [1926] (2 I.T.C. 173).

LACHIRAM BASANTLAL, *In re* [1931] (58 Cal. 909; 35 C.W.N. 310; 133 I.C. 187; A.I.R. 1931 Cal. 545).

MADAN MOHAN LAL *v.* COMMISSIONER OF INCOME TAX PUNJAB [1935] 16 Lah. 937; 38 P.L.R. 52; 158 I.C. 718; 1935 Lah. 742; 1935 I.T.R. 438).

RAJENDRANATH MUKHERJI v. COMMISSIONER OF INCOME TAX, BENGAL [1934] (61 I.A. 10; I.L.R. 61 Cal. 285; 147 I.C. 663; 1934 P.C. 30; 1934 I.T.R. 71).

RAMJIDAS MAHALIRAM, *In re* [1935] 62 Cal. 1011; 1936 I.T.R. 25).

E. W. Lambert, for the Commissioner of Income-tax.

De, for the Assessee.

PAGE, C. J.—The question propounded is "whether the re-assessment in this case was in accordance with the provisions of Section 34 of the Act?" Section 34 runs as follows:

"34. If for any reason income, profits or gains chargeable to income-tax has escaped assessment in any year or has been assessed at too low a rate, the Income-tax Officer may, at any time within one year of the end of that year, serve on the person liable to pay tax on such income, profits or gains, or, in the case of a company, on the principal officer thereof, a notice containing all or any of the requirements which may be included in a notice under sub-section (2), of Section 22 and may proceed to assess or re-assess such income, profits or gains, and the provisions of this Act shall, so far as may be, apply accordingly as if the notice were a notice issued under that sub-section: Provided that the tax shall be charged at the rate at which it would have been charged had the income, profits or gains not escaped assessment or full assesment, as the case may be".

The question is not happily framed and is too wide, the substance of it having regard to the matter in controversy being whether there were any materials upon which the Income-tax Officer or the Assistant Commissioner could find that the income, profits and gains which were the subject of the assessment under Section 34 had escaped assessment in the year 1931-32.

The material facts lie within a narrow compass. Up till January, 1932, the business of a chemist and druggist in Mogul Street, Rangoon, was carried on in partnership by the Dey brothers, a manager appointed by the elder brother, Dr. Dey being in charge of the business. After January, 1932, the younger Brother, L. M. Dey who is the assessee, became the sole proprietor and employed a different manager to carry on the business for him. The assessment order of the Income-tax Officer in respect of the year 1931-32, was passed on 16th June, 1931, in the following terms:

"The books have been scrutinized, and the return checked and found in order. I accept the return of income, *viz.*, Rs. 8,267. Tax thereon at 9 pies in the rupee is Rs. 387-8. Issue demand-notice payable in one month.

(*Sd.*) S. E. Trutwein,
Income Tax Officer."

16th June, 1931.

Thereafter as the result of a search upon the premises certain documents came into the possession of the Income-tax Department, in consequence of which the manager was prosecuted and convicted on 12th June 1933 of submitting *inter alia* a false income-tax return; but the convictions were set aside on appeal by DUNKLEY, J., on 12th July 1933. If the proceedings under Sec. 34 which were commenced on 5th July, 1932 could have been delayed until after the judgment of DUNKLEY, J., had been passed, it may be that they would not have been set in motion, for the learned Judge held that there was "no evidence that the appellant intentionally submitted a false return to the Income-tax Officer." However, the proceedings under Section 34, which before that time had been completed, resulted on 19th August 1932 in an assessment being made on a total income of Rs. 68,267 instead of Rs. 8,267 under the original assessment. The assessment was set aside after a reference to the High Court under Section 66 (3), and on 22nd February, 1935 the Commissioner of Income-tax directed the Income tax Officer to open fresh proceedings, presumably under Section 34. On 10th May, 1935, the Income-tax Officer accepted the following figures for cash sales in the years 1930-31, 1932-33 and 1933-34:

Year	Sales	Gross profit	Percentage of gross profit
	Rs.	Rs.	Rs.
1933-34	2,29,256	47,780	20.8
1932-33	2,57,067	63,599	24.7
1930-31	3,07,335	43,457	14.1

In the assessment order the Income-tax Officer observed:

"A comparison of these figures shows that, according to the accounts produced by the firm, the percentage of gross profit in 1930-31 was 14.1 compared with 24.7 in 1932-33 and 20.8 in 1933-34. The sales however, in the year 1930-31, in which the gross profit was smallest, were larger than those in the other two years. The result of the trading for the year 1930-31 as disclosed by the books produced cannot therefore be accepted off-hand,

The Income-tax Officer rejected the explanation of the assessee that "the reason for the gross profit being only 14.1 per cent is said to be due to keen competition between the assessee firm and the Grand Pharmacy which is stated as having commenced business about this year (1930-31)," and merely because the figures in the latter years showed a larger profit on a smaller turn-over the Income-tax Officer arbitrarily estimated that 30 per cent. of the figure for sales in 1930-31 must have represented the gross profit and he assessed the income, profits and gains of the assessee upon that footing. On appeal the Assistant Commissioner reduced the assessment from Rs. 59,130 to Rs. 40,180, but otherwise affirmed assessment, stating that "the main ground for the rejection of the accounts remains, namely, that the analysis of the trading account shows a rate of gross profits which is substantially below the rates shown in subsequent accounts. And it is this Department's case that this result is due to an understatement of the closing stock for the year. The following table sets out the trading results for the relevant years as shown in the firm's accounts.

Assessment year	Opening Stock	Purchases	Sales	Closing Stock	Gross Profit	Percentage
(1)	(2)	(3)	(4)	(5)	(6)	(7)
	Rs.	Rs.	Rs.	Rs.	Rs.	
1930-31	1,41,874	2,82,755	3,60,862	1,11,822	48,054	13.3
1931-32	1,11,822	2,40,477	3,07,335	88,421	43,457	14.1
1932-33	88,421	2,01,722	2,67,796	60,910	38,563	14.4
1933-34	60,910	1,94,511	2,57,068	61,951	63,598	24.7
1934-35	61,951	1,83,754	2,29,256	64,228	47,779	20.8

These figures show a marked increase in the gross profits for the years 1933-34 and 1934-35, and this is significant for the accounts for these years were submitted after the prosecution referred to in para. 2 above was launched. Before considering what, in my opinion, should be the answer given to the question referred I desire to observe, with all due respect, that I cannot agree with the following passages in the judgment of the Bombay High Court in *Commissioner of Income-tax, Bombay* v. *Gopal Vaijinath Manohar* :—

"It seems to me that the burden of showing that income has escaped assessment or that it has been assessed at too low a rate, lies on the Commissioner."

and

"I think the burden of proving that the income has escaped assessment within the meaning of Sec. 34, Income-tax Act, was on the income-tax authorities, and it has clearly not been discharged."

If BEAUMNOT, C.J., and RANGNEKAR, J., intended to lay down that under Section 34 the onus lay upon the income-tax authorities to satisfy the Court upon the facts that income, profits and gains had escaped assessment, the effect of so holding would be that in every case in which proceedings are taken under Section 34, the assessee would have an appeal upon the facts. That in my opinion was neither intended nor provided; and I apprehend that under Section 34, if the income-tax authorities have not misdirected themselves in law, and there were any materials before they could find that income, profits and gains had in fact escaped assessment the Court will not interfere or disturb the finding of fact at which the income-tax authorities have arrived.

Further, I am of opinion that the animadversions passed by the Bombay High Court in *Commissioner of Income tax, Bombay* v. *G. V. Manohar* upon certain observations of a Bench of this High Court in *U Lu Nyo's case* were not justified. The learned Judges who decided *Commissioner of Income-tax, Bombay* v. *G. V. Manohar* while agreeing with the actual decision in *U Lu Nyo's case* appear to have been under the impression that in *U Lu Nyo's case* this Court had held that "income from a particular source cannot be re-assessed under Seetion 34." With all due respect the Court in *U Lu Nyo's case* did not, and did not purport to lay down the law in that sense. In *U Lu Nyo's case* as in *Commissioner of Income-tax, Bombay* v. *G. V. Manohar* an Income-tax Officer in a subsequent year of assessment, arriving at a different estimate of the income that had accrued in the previous year from that at which the Income-tax Officer in the previous year had arrived, proceeded to re-assess under Section 34, the difference between the amount of the two estimates as being income that had "escaped assessment" in the previous year. That we held to be an attempt by one Income-tax Officer to go behind and revise the assessment made by the Income-tax Officer in the previous year, merely because he disagreed with his predecessor's estimate of the amount of the assessable income.

In that connection the Court laid down that "the Income-tax Officer had no jurisdiction to revise the assessment for the previous year which was completed and had become final." We respectfully adhere to what was said in *Commissioner of Income-tax,*

Burma v. *U. Lu Nyo* for in our opinion income in respect of which a final and conclusive assessment has been made cannot be subjected to re-assessment, except when the assessment has been fixed at too low a rate, either under Section 34 or any other section of the Income-tax Act. The view which the Court expressed in *U Lu Nyo's case* and which finds favour with us, appears to receive confirmation from the following observations of Lord Macmillan in *Rajendranath Mukerjee* v. *Commissioner of Income-tax, Bengal :*

'The fact that Section 34 requires a notice to be served calling for a return of income which has escaped assessment strongly suggests that income which has already been duly returned for assessment cannot be said to have escaped assessment within the statutory meaning.'

It may be necessary, of course, in certain cases to examine income *A*, which has already been duly assessed, in order to ascertain whether income *B* has escaped assessment, but that does not mean that income *A* is liable to be re-assessed under Section 34; and we are firmly of opinion that income, profits and gains that have already been duly assessed and the assessment in respect of which has become binding and conclusive cannot be subjected to a revised assessment under Section 34 except where the rate originally charged was too low. On the other hand we are equally clearly of opinion, and as we understand the judgment in that case there is nothing to the contrary in *U Lu Nyo's case* that income, profits and gains liable to assessment but which have not been assessed in the year of assessment in which they are chargeable, whether or not they are derived from the same source as income that has been so assessed, are within Section 34 and are liable to be assessed within the period prescribed in that section as being income, profits and gains that have escaped assessment, *Commissioner of Income-tax, Burma* v. *T. S. T. S. Chettyar Firm, Commissioner of Income-tax,* v. *U Lu Nyo, In re Lachiram Basantlal, In re Anglo Persian Oil Co., (India) Ltd., Burn & Co., In re, Rajendranath Mukerjee* v. *Commissioner of Income-tax, Bengal, In re Ramjidas Mahaliram, Commissioner of Income-tax, Madras* v. *R. Sundaresa Iyer, Madan Mohan Lal* v. *Commissioner of Income-tax, Punjab* and *Commissioner of Income-tax, Bombay* v. *G. V. Manohar.*

In my opinion the true rule was enunciated in *Commissioner of Income-tax, Burma* v. *N. N. Burjorjee* where the Court held

that Section 34 is applicable to cases in which either no assessment at all has been made upon the person who received the income, profits or gains liable to assessment, or where an assessment has been made in the course of the year, but some portion of the income, profits or gains of such assessee for some reason or other has not been included in the order of assessment; such income is income which has "escaped assessment" in the year, and falls within the ambit of Section 34 of the Act.

Now, applying Section 34, construed in this sense, to the facts of the present case I am of opinion that there was no material before the income-tax authorities upon which they could have found that any income, profits and gains were liable to assessment under Section 34. Upon the footing that the table of figures compiled from the assessee's books of account was accepted, and the additional assessment was based upon the ground that commended itself to the Income-tax Officer, namely, that because from the figures for later years it is clear that a larger gross profit was therein made on a smaller turnover than in the accounting year, I am not satisfied that it follows that in the accounting year the the gross profit must have been greater than the profit returned by the assessees. It appears to me that this conclusion cannot be drawn from the premises, and that the argument involves a non-sequitur. It is at least equally probable that the larger profit accruing in the later years was due to the absence of trade competition or to better management—for it must be remembered that in the subsequent years the assessee was the sole proprietorof the business and that it was under new management—as that there was no increase in the profits of the later years, and in my opinion in such circumstances there were no materials from which the Income-tax Officer could have found that in the accounting year there were profits from the business which had "escaped assessment."

On the other hand, if the figures returned by the assessee were rejected *in toto* there were *ex necessitate rei* no material from which the inference drawn by the income-tax authorities could have been deduced; and even if assuming that the income tax authorities were justified in the circumstances in coming to the conclusion that the value of the "closing stock" was based not on its true value to the assessee but on the "invoice" price, without taking into account, for example, the cost of freight, or import duty, it does not follow that the calculation of the gross profit as returned

was incorrect unless the value of the "opening stock" had been otherwise and/or truly assessed. But not only was there no evidence before the Income-tax authorities that the "opening stock" and the "closing stock" were not valued on the same basis, but from the table itself it appears that in each year the "opening stock" stood at exactly the same figure as the "closing stock" of the previous year, a fact which would militate against the view that the "opening stock" and the "closing stock" in the return of the assessee for the year of assessment had not been valued in the same way. In my opinion the assessment that has been made under Section 34 has been based not upon facts, but upon surmises and hypotheses for which there is no sound foundation, and, in my opinion, the assessment under Section 34 cannot be sustained. I would answer the question propounded in the negative. The assessee is entitled to costs 10 gold mohurs including Rs. 100 deposited.

MYA BU, J.—I agree.

BA U, J.—I agree.

Reference answered accordingly.

[IN THE LAHORE HIGH COURT.]

BANARSI DAS

v.

COMMISSIONER OF INCOME TAX, PUNJAB & N. W. F. P.

SIR JAMES ADDISON and ABDUL RASHID, JJ.

January 27, 1936.

PENALTY—BEST JUDGMENT ASSESSMENT—APPEAL TO ASSISTANT COMMISSIONER—POWER OF ASSISTANT COMMISSIONER TO IMPOSE PENALTY AFTER REJECTING APPEAL—POWER OF COMMISSIONER TO IMPOSE PENALTY IN FURTHER APPEAL OR ON APPLICATION FOR REFERENCE—INDIAN INCOME TAX ACT (XI OF 1922), SECTIONS 23 (4), 28 (3), 30, 32 AND 66 (2).

Where an Assistant Commissioner refuses to admit an income tax appeal on the ground that the assessment being an assessment under Section 23 (4) no appeal lies, the proceedings before him come to an end and he has no power to issue a notice under Section 28 (3)

calling upon the assessee to show cause why a penalty should not be imposed on him.

Where the Assistant Commissioner imposes a penalty in such a case and the assessee appeals to the Commissioner complaining against the illegal imposition of penalty by the Assistant Commissioner, the Commissioner cannot himself re-impose the penalty and thereby validate the very order which was being challenged before him.

The Commissioner is also precluded from imposing a penalty in such a case when an application is preferred to him under Section 66 (2) praying that he may refer to the High Court the question of the validity of the imposition of the penalty by the Assistant Commissioner.

Further, no penalty can be imposed under Section 28 of the Act unless a notice is served on the assessee to show cause against the imposition of such a penalty.

Reference (No. 20 of 1935) made by the Commissioner of Income-tax, Punjab & N. W .F..P., under Section 66, Clauses (1) and (2), of the Indian Income-tax Act (XI of 1922) in the matter of the assessment of *Rai Bahadur* Lala Banarsi Das of Ambala for the year 1933-1934.

The necessary facts appear in the Judgment.

Achru Ram and *Asa Ram Aggarwal*, for the assessee.

Jagannath Aggarwal, for the Commissioner.

ORDER.—Under the provisions of Section 66 (1) and (2) of the Indian Income-tax Act the Commissioner of Income-tax, Punjab, has referred the following questions to this Court:—

1. *Commissioner's First Question.*

Was there any material before the Commissioner on which he could uphold in appeal the finding that the assessee had concealed and deliberately furnished inaccurate particulars of income and thereby returned it below its real amount?

2. *Commissioner's Second Question.*

Is the maximum penalty admissible under Section 28 restricted in law otherwise than by the difference between the income-tax upon the total income actually returned and that upon the total income actually assessed?

3. (a) *Assessee's First Question.*

Whether in a case held as validly decided under Section 23 (4) by an Assistant Commissioner of Income-tax, is he lawfully

competent to impose any penalty under Section 28 (1) of the Income Tax Act?

(b) Assessee's Second Question.

Whether in the circumstances of the case there were any proceedings before the Assistant Commissioner of Income tax within the meaning of Section 28 (1) of the Act.

(c) Assessee's Third Question.

Whether the issue of the notice under Section 28 (3) on 20th April, 1934, and imposition of the penalty on 30th April, 1934, by the Assistant Commissioner are valid in law under Section 28 of the Income Tax Act when he refused to admit the appeal on 18th April, 1934.

(d) Assessee's Twelfth Question.

Whether the imposition of surcharge of Rs.4,506-11-0 is legal in the calculation of penalty under Section 28 (1) of the Act.

The material facts of the case may be briefly stated. The assessee, *Rai Bahadur Lala* Banarsi Das, returned his income for the year 1932-33 at Rs. 79,807-0-0. The Income Tax Officer made the assessment for the year 1933-34 at the sum of Rs. 2,12,927-0-0 under Section 23 (4) of the Act on the ground that the Gunny Bag Godown Register and the Gunny Bag Register of receipts and issues specifically called for under Section 23 (2) had been deliberately withheld by the assessee. The assessee preferred an appeal to the Assistant Commissioner. The principal ground of appeal was that the Registers which, according to the Income Tax Officer, had been deliberately withheld were not maintained, and that the non-production of a document not maintained was not a default and did not bring the case of the assessee within the ambit of Section 23 (4) of the Income Tax Act. It was contended that the order of the Income Tax Officer was in reality an order under Section 23 (3) of the Act, and that it was labelled as one under Section 23 (4) in order to deprive the assessee of his right to appeal.

The Assistant Commissioner in his order dated the 18th of April, 1934, came to the conclusion that the registers in question had been deliberately withheld and that in view of these facts the assessment made by the Income Tax Officer under Section 23 (4) was valid, and that the order of the Income Tax Officer was consequently not appealable. The order of the Assistant Commissioner concludes with the following words:—

"The present appeal is therefore, *not admitted*. The other objections relate to the merits of the case and so need no discussion.

"I also find that the appellant returned no income from the *Bardana* (Gunny Bags) *Khata*, although it has been found by the Income Tax Officer that he has got substantial income under this head. I have, therefore, issued a notice as required by Section 28 (3) of the Income Tax Act calling upon the appellant to show cause why action should not be taken against him under Section 28 (1) of the said Act. The question of imposing of penalty will be finally decided after hearing the appellant."

By his order, dated the 30th of April, 1934, the Assistant Commissioner held that on the assessee's own admission the Gunny Bags account did yield an income of Rs. 33,372-0-0 which he had failed to return, and that, therefore, the assessee was liable to penalty under Section 28 of the Act. The penalty of Rs. 22,533-6-0 was consequently payable by the assessee. Against the decision of the Assistant Commissioner imposing the penalty the assessee preferred an appeal to the Commissioner. This appeal was rejected on the merits and the order of Assistant Commissioner was confirmed, but under Section 66 (2) of the Act the Commissioner has referred to this Court the question of the validity of the imposition of penalty which forms the subject matter of assessee's first three questions.

The Income Tax Officer completed the assessment on the 31st of January 1934. The assessment order contains an observation to the effect that the assessee had deliberately made a false return inasmuch as he had omitted to show the income in the Gunny Bags account and that separate action under Section 28 or 52 was being taken. In spite of this observation, however, the Income Tax Officer took no action on the 31st of January 1934 or at any time thereafter by issuing a notice to the assessee under Section 28 of the Income Tax Act. According to the Commissioner, the case was submitted to the Assistant Commissioner by the Income Tax Officer on the 14th of March 1934, recommending prosecution but no action appears to have been taken on that recommendation. It was contended by the learned counsel for the assessee that the Assistant Commissioner became *functus officio* as soon as he passed order, on the 18th of April 1934, to the effect that the assessment under Section 23 was valid and that the order of

the Income-tax Officer was not appealable. The Assistant Commissioner "did not admit the appeal." All proceedings before him, under the Income-tax Act, ended as soon as that order was passed.. After passing that order the Assistant Commissioner had no power to issue a notice under Section 28 (3) to the assessee as his power to take action under Section 28 lasts only so long as any proceeding under the Income-tax Act are pending before him. This contention, in our opinion, is sound and must be given effect to. The Commissioner has observed that in his opinion the determination of the issue raised under Section 30 was manifestly in the course of proceeding under that Section. Section 30 deals with appeals against assessments and as soon as the Assistant Commissioner found that the assessment was validly made under Section 23 (4), the proviso to Section 30 (1) came into operation, and it was in pursuance of that proviso that the Assistant Commissioner refused to admit the appeal. The issue raised under Section 30 was, therefore, conclusively determined as soon as the Assistant Commissioner refused to admit the appeal, and thereafter, the Assistant Commissioner could not take any action under Section 28 (3) by issuing a notice to the assessee regarding penalty.

The learned Commissioner has further held that he has himself duplicated the order regarding the penalty in the proceedings under Section 32 and Section 66 (2) so that the decision of the above question as to the jurisdiction of the Assistant Commissioner would not affect the penalty. Section 32 deals with appeals preferred to the Commissioner against certain orders of the Assistant Commissioner. In the present case the assessee appealed to the Commissioner urging that the imposition of the penalty by the Assistant Commissioner was illegal as the concealment of income, if any, did not come to his notice during the course of any *proceedings* before him. The Commissioner in deciding whether the imposition of the penalty by the Assistant Commissioner was illegal could not, in our opinion, re-impose the penalty himself, and thereby validate the very order which was challenged in appeal before him. For the same reason the application was preferred to him under Section 66 (2) of the Act praying that he may refer to the High Court the question of validity of the imposition of the penalty by the Assistant Commissioner.

No penalty can be imposed under Section 28 of the Act unless a notice is served on the assessee to show cause against the imposi-

tion of such a penalty. The Commissioner never served any notice on the assessee that he intended to take action against him under Section 28. An imposition of penalty in this case by the Commissioner under Section 28 would, consequently, be invalid. We therefore, answer the first three questions of the assessee referred by Commissioner in the negative.

In view of the finding given above, it was stated by the learned counsel for the assessee that he did not wish to argue the other questions and that they may be answered in accordance with the opinion of the Commissioner. We answer them accordingly. We order that the parties shall bear their own costs in this reference.

Order accordingly.

[IN THE LAHORE HIGH COURT.]

BHIWANI SAHAI BISHAMBAR DAYAL

v.

COMMISSIONER OF INCOME TAX, PUNJAB, N.W.F.P. AND DELHI.

Sir James Addison and Abdul Rashid, JJ.

April 7, 1936.

ACCOUNT BOOKS—ACCOUNTS OF FOREIGN BUSINESS - NON-PRODUCTION—POWER TO MAKE SUMMARY ASSESSMENT—POWER TO ISSUE COMMISSIONS—REFERENCE—SUFFICIENCY OF CAUSE FOR NON-PRODUCTION—WHETHER QUESTION OF FACT—INDIAN INCOME TAX ACT (XI OF 1922), SECTIONS 23 (3), 37, 66 (2).

Where there was evidence to show that the assessee had the whole or a predominating interest in a business carried on outside British India and the assessee refused to produce the account books relating to that business or even copies thereof and there was nothing to show that the account books were not under his control or that he could not have had access to them: Held, *that the income tax authorities were entitled to require the assessee to produce the accounts of his foreign business for determining the profits made therein and to make an assessment under Section 23 (4) on his refusal to produce them*:

Usually the sufficiency of cause for non-production of account books is a question of fact but it may involve a question of law.

It is not proper to threaten or warn an assessee that unless he produced his account books he would be assessed at a particular figure. The question of quantum *must be dealt with in a liberal spirit.*

Section 37 of the Indian Income-tax Act does not empower income-tax authorities to issue a commission for examination of books; it gives power only to issue commission for examination of witnesses.

Case stated by the Commissioner of Income-tax, Punjab, N. W. F. P. and Delhi under Section 66 (2) of the Indian Income-tax Act (Ref. No. 2 of 1936).

Mehr Chand Mahajan and *Kirpa Ram Bajaj*, for the assessee.
Jagan Nath Aggarwal, for the Commissioner of Income-tax.

JUDGMENT: Under Section 66 (2) of the Indian Income-tax Act the Commissioner of Income-tax, Punjab, has stated the case of the Hindu undivided family of Bishamber Dayal and his sons, and referred the following questions of law in connection therewith for the opinion of this Court:—

1. Is the sufficiency of cause shown under Section 27 of the Act an issue of law within the scope of Section 66 (2) of the Act?

2. If the above be answered in the affirmative, is it possible in law for the Income-tax Officer to find that sufficient cause had not been shown preventing the assessee from producing the books of Malwa Cotton Press of Ujjain, Gwalior State?

The assessment under consideration is that of the year 1931-32. Owing to various reasons this assessment was not made till the 25th October, 1933 and when it was made the assessment was under Section 23 (4) of the Act. There was an application under Section 27 to set aside this assessment which was rejected on the 15th May 1934, an appeal therefrom being dismissed on 31st May 1935. The assessee then moved the Commissioner in connection with the order passed in appeal.

The assessment included certain local businesses in the Punjab as to which there is no contest. The dispute relates solely to the business 'Malwa Cotton Factory' (press), at Ujjain in Gwalior State outside British India, income from which was included at an estimated amount of Rs. 40,000. It was for non-production of the books of that factory that the assessment was

made under Section 23 (4). The assessee put forward two contentions before the Commissioner, namely, that the share in that factory belonged to Bishamber Dayal individually and not to the assessee family, and that in any event the books could not be produced to show that there were no remittances of income therefrom in the period under assessment.

Bishamber Dayal used to be joint with his brother but in 1928-29 their separation was established under Section 25-A of the Act. The existence of the cotton press in question came to light only in the 1926-27 assessment, though admittedly it had been a source of income from at least 1921. Since 1926-27 the income tax authorities have made every attempt to obtain correct information from the assessee as to the interest of the family in that press. They have also tried since then to have the books brought before them or even certified copies of the accounts, but the assessee has complied with none of these requests. The assessee family have been pleading that the account books of the press are not in their control and that they have been unable to induce the persons in charge of the business to lend them the required books for the purposes of their assessment. For this reason the main contention before us was that the notice under Section 22 (4) of the Act to produce the account books of Ujjain was *ultra vires*, and that therefore the assessee had been prevented by sufficient cause within the meaning of Section 27 of the Act from complying with the terms of the notices issued by the Income-tax Officer. The assessee or the Advocate appearing for him before the Income-tax Officer, was not prepared to disclose the constitution of the press, to produce a copy of the profit and loss account or even the assessee's ledger account, while it was known to the income tax authorities that Bishamber Dayal was going there four or five times a year and had a considerable interest in the affairs of the press. That interest was said to be a one anna share in 1928-29, in a statement made by the assessee's Advocate but in 1929-30 the *munim* of the firm admitted that the share was at least 2/16ths. This *munim* added that the share had existed for the last four or five years, whereas as a matter of fact Bishamber Dayal had an interest in the press since 1921 at least, the exact date being unknown because of the action of the assessee in withholding all information about the press. During the course of the application under Section 27 the Income-tax Officer on a request made to him twice summoned the manager and the accountant of the press but they did not appear.

Bishamber Dayal and his eldest son, whom the Income-tax Officer also summoned, did not appear while their Advocate did not produce the documentary evidence which he had promised to furnish. All these facts are significant and were rightly taken into account by the Commissioner.

It was contended before us that under the provisions of Section 37 of the Income-tax Act, the Income-tax Officer should have issued a commission for the examination of the books of the press at Gwalior. Section 37 of the Act, however, does not give such power: apparently it gives power only for the examination of witnesses. We agree that it would have been useless to issue a commission to examine the manager of the factory as a witness at Gwalior; for, without the books, or a copy thereof, such examination would be futile. Under Section 12 (d) of the Indian Partnership Act, every partner has a right to have access to and to inspect and copy any of the books of the firm. Bishamber Dayal, however, consistently refused to produce the books, or to have the books produced, or to give any information whatsoever with respect to the press, while the income tax authorities have done everything they could to try and get information with respect to the press.

The main contention before us was that the books were not within the power of Bishamber Dayal and that therefore there was sufficient cause for not complying with the terms of the notices of the Income-tax Officer. It is the case that the books of a partnership are usually kept at the headquarters thereof, but there is nothing to prevent them being taken to another place for a temporary purpose. The terms of the partnership are not known and it may be the case that no provision has been made about the keeping of books at the headquarters, while, as already pointed out, Bishamber Dayal was entitled to copy them *in toto*. He has sheltered himself under the allegation that the books are not in his power, but at various stages he was given opportunities to produce copies thereof and this he could certainly have done. He has also not shown that there is any dispute between him and the alleged manager which would cause the latter to refuse to produce the books or to abstain from giving any information whatsoever. It has been established that Bishamber Dayal goes frequently to the factory and must thus be in friendly relations with the management. From local inquiries it is supposed to be the main source of the family's income. In view of what has been said above, the failure to furnish any details of the alleged partnership, the complete absence of any details of any dispute with the other partners,

if any, and the failure to produce any documents in connection with the partnership it seems to us that the income tax authorities were justified in concluding that the assessee owns the whole concern or an indistinguishable predominating interest and control therein.

On this finding the case falls within the four corners of *Mahomed Kasim Rowther* v. *Commissioner of Income Tax, Madras* (59 M. L. J. 220; 4 I. T. C. 427). The assessee in that case was a resident of British India with a known share namely four fifths in a business carried on in Penang with a non-resident. He was required by the Income Tax Officer to produce all the original accounts of the Penang business. On non-compliance with the requisition an assessment was made under Section 23 (4), the alleged refusal of the non-resident partner to produce the accounts not having been believed by the Income Tax Officer. It was held that the Income Tax Officer was entitled to require the production of the accounts of the foreign business which would be relevant for determining the quantum of profits made therein, and that on the finding that the accounts called for were under the control of the assessee who could have produced them, the assessment was legal. In the present case there is evidence on which the Income tax authorities were justified in concluding that the assessee had the whole or a predominating interest in the concern, and it follows, therefore, that he could have produced the books. The answer to the second question referred must be in the affirmative.

The first question referred is an abstract question of law divorced from facts and need not be replied to. It is sufficient to say that usually the sufficiency of cause is a question of fact. It is, however, unnecessary to lay down that in no circumstances can a question of law ever arise. Two important cases with reference to this subject are 5 I. T. C. 352 and 8 I. T. C. 472.

Before sending the case back to the Commissioner there is one other matter we desire to mention. The Income Tax Officer noted that he had warned the assessee that he would estimate the Ujjain income at Rs. 40,000-0-0 if the books were not produced. As has very properly been pointed out by the Commissioner, the phrasing of the Income Tax Officer may seem to imply something of a threat and the Commissioner regreted the unfortunate implication of the phrase. Because of this remark the Commissioner has very properly stated that if this Court's decision on the questions stated left the matter one of estimate (as it does) he would be

prepared under Section 33 to examine the quantum more fully, though he was satisfied that the estimate was not perverse. We note with approval this remark and have no doubt that the Commissioner will deal with the question of quantum in a liberal spirit. The Commissioner will have his costs here.

Reference answered.

[IN THE JUDICIAL COMMISSIONER'S COURT OF SIND.]

COMMISSIONER OF INCOME TAX, BOMBAY

v.

TEJBHANDAS MOTUMAL.

RUPCHAND, A. J. C., and MEHTA, A. J. C.

February 10, 1936.

INCOME TAX—APPEAL TO PRIVY COUNCIL—CONDITIONS FOR GRANTING LEAVE TO APPEAL—PARTNERSHIP—INTEREST PAID ON CONTRIBUTION BY PARTNER—WHETHER ALLOWABLE DEDUCTION—DISTINCTION BETWEEN CONTRIBUTION AND LOAN—APPEAL INVOLVING SMALL AMOUNT—POWER OF COURT TO DIRECT APPELLANT TO PAY COSTS IRRESPECTIVE OF RESULT OF APPEAL—INDIAN INCOME TAX ACT (XI of 1922), SECTIONS 10 (2) (iii), 66-A (iii).

A partnership agreement provided that the capitalist partners shall contribute rupees one lakh out of which the partnership was to pay interest on Rs. 94,900 at the rate of 6 per cent. per annum and the balance of Rs. 5,100 was not to carry any interest. The firm paid Rs 7,721 by way of interest to the capitalist partners in respect of money advanced by them over and above Rs. 5,100 and claimed that in assessing its profits this sum must be deducted. The Judicial Commissionor's Court held that this amount was an admissible deduction. The Commissioner applied for leave to appeal to the Privy Council:

Held, *that the question whether this amount of Rs. 7,721 could be deducted was not a question of any great public or any private importance and leave could not therefore be granted for appeal to the Privy Council.*

Before the High Court can grant leave to appeal to the Privy Council in an income tax case it should be satisfied that the

case is of such importance as would warrant a certificate under Section 109 (c) of the Civil Procedure Code.

Section 10 (2) (iii) of the Indian Income Tax Act makes a distinct departure from English Law which provides that interest on capital employed in business is not an allowable deduction.

As the pecuniary amount involved in several income tax cases in small and it may be difficult for the assessee concerned in a particular case to incur the expense of appearing before the Privy Council, it is desirable that the legislature should confer a power on the High Courts to impose a condition in a fit case, requiring the appellant to the Privy Council to bear the costs of the appeal irrespective of the result of the appeal, at the time of granting leave to appeal.

Cases referred to:

BOLASHAH *v.* COMMISSIONER OF INCOME TAX, [1930] (A.I.R. 1930 Lah. 738; 126 I.C. 142).

CLARKE *v.* BRAJENDRA KISHORE [1909] (13 C.W.N. 1127; 2 I.C. 786).

COMMISSIONER OF INCOME TAX, *v.* BULCHAND KESHAVDAS [1933] (A.I.R. 1933 Sind 344; 148 I.C. 161; 1934 I.T.R. 197).

COMMISSIONER OF INCOME TAX *v.* SUBRAMANIAM CHETTIAR [1928] (51 Mad. 787; 1928 Mad. 923; 110 I.C. 889; 55 M.L.J. 416; 3 I.T.C. 157).

DELHI CLOTH & GENERAL MILLS CO. *v.* INCOME TAX COMMISSIONER [1927] (54 I.A. 421; 1927 P.C. 242; 106 I.C. 156).

INDIAN IRRIGATION TRUST BOARD OF NATAL *v.* GOVINDASWAMI [1921] 1 A.C. 433; 90 L.J.P.C. 38; 37 T.L.R. 128; 124 L.T. 643).

RAJA RAJESWARA SETHUPATHI *v.* TIRUNEELAKANTAM SERVAI [1923] (44 M.L.J. 217; A.I.R. 1923 Mad. 232; 32 I.C. 250).

SIBNARAIN GHOSE, *In re* [1851-54] (5 M.I.A. 322; 3 Moore P.C. 276; 1 Sar. 448).

SPOONER *v.* JUDDOW [1846-50] (4 M.I.A. 353; 6 Moore P.C. 257; 1 Sar. 363).

Application for leave to appeal to the Privy Council from a judgment of the Judicial Commissioner's Court of Sind reported as *Commissioner of Income Tax, Bombay* v. *Tejbhandas Motumal* (1933 I.T.R. 202). Privy Council Application No. 42 of 1933.

G. M. Lobo, for the Commissioner of Income Tax.

Kimatrai Bhojraj, for the assessees.

RUPCHAND BILARAM, A. J. C.—The facts giving rise to the present application are somewhat as follows: The respondents are a firm carrying on business under the terms of a partnership agreement which contains *inter alia* the following clause:

'The capitalist partners of the first part shall contribute to the partnership Rs. 1,00,000 (one lac), out of which the partnership shall pay interest on Rs. 94,900 at the rate of 6 per cent. per annum. The balance of Rs. 5,100 shall not carry any interest. It is optional with the capitalist partners to advance further capital if they so chose in which event the further advances shall also carry interest to be borne by the partnership at the same rates as above said.'

The firm claimed that in assessing its profits for the purposes of income-tax they were entitled to deduct two items of Rs. 2,166 and Rs. 5,555 paid by them to the capitalist partners in respect of money advanced by them during the period under assessment over and above Rs. 5,100 which was advanced by them free of interest. In support of their contention they relied upon the provisions of Section 10, Clause 2, sub-clause (iii) of the Act. Their plea was disallowed and on a request made by them to the Commissioner of Income-tax to make a reference to this Court under Section 66 (2) of the Act he referred the following question to the Court for decision:

'Whether in the circumstances of the case the two items of Rs. 2,166 and Rs. 5,555 aggregating in all to Rs. 7,721 paid as interest to the capitalist partners during the accounting period on account of capital invested in the business can be allowed as items of expenditure under the provisions of Section 10 (2) (iii) of the Act.'

The decision of the Court on the above question is:

'That the firm is entitled to credit for both these items and that their taxable income should be assessed after giving them credit for these two items.'

The amount by which the respondents have benefited by this decision is in the vicinity of Rs. 300 and we are asked to certify under Section 66-A, Clause (iii), Income-tax Act, that this is a fit case for leave to appeal to His Majesty in Council. In *Delhi Cloth and General Mills Co.* v. *Income-tax Commissioner, Delhi*, their Lordships of the Privy Council have held that a High Court is justified in refusing a certificate in a case which in its view does not raise any of such contentions as would warrant a certificate

under Section 109 (c), Civil Procedure Code, 1908; and therefore before we grant leave in the present case we should be satisfied that this is a case of such importance as would warrant a certificate under Section 109, Clause (c), Civil Procedure Code. The reference submitted by the Income-tax Commissioner to us under Section 66, Clause (2) and the decision given by us are *prima facie* not of public importance much less of great public importance or of great private importance. In the statement of the case submitted to us by the Income-tax Commissioner he did not dispute the correctness of the rulings given by the Madras and Lahore High Courts in *Commissioner of Income-tax* v. *Subrahmaniam Chettiar*, and *Bholashah* v. *Commissioner of Income-tax*. But he attempted to distinguish these cases by observing:

'These two cases clearly dealt with money lent by a partner beyond the initial capital and not with the initial capital subscribed to the partnership . . . Hence the Commissioner is respectfully of opinion that interest has been paid in this case not on account of initial capital subscribed to the partnership by the capitalist partner. It is this very fact of their having subscribed capital to the partnership that they are designated as capitalist partners.'

The learned Income-tax Commissioner draws a distinction between capital advanced at the commencement of the partnership and that advanced subsequently. But so far as that distinction is concerned there was nothing on the record submitted to us to show that the whole sum of money on which rebate was claimed was advanced at the very commencement of the partnership so as to justify the use of the expression "initial capital." All that para. 3 of the partnership agreement contemplated was a promise by the capitalist partners to advance to the extent of Rs. 1 lac of which Rs. 5,100 was to carry no interest and the rest to carry interest at 6 per cent. per annum. The capitalist partner was entitled to receive interest on the excess whether there was profit or loss in the business, and he was to get this in addition to his share of the profit. The fact that the partnership agreement contained a proviso that the capitalist partner was bound to advance up to a certain limit, money on interest did not make such money initial capital or render the money advanced by him capital contributed as opposed to capital borrowed. The question raised by the learned Commissioner affected the particular assessee and depended upon the construction of the particular agreement. It was perhaps possible for the learned Commissioner to have so framed his

question as to make it a question of great importance and depending upon general principles, but that is not what he has done in this case. Grounds (a), (b) and (e) in the application for leave to appeal to His Majesty in Council are these:

(*a*) That the learned Judicial Commissioners erred in holding that the assessee firm was entitled to a deduction on account of the above mentioned two items and that their taxable income should be assessed after giving them a deduction for the two items.

(*b*) That the learned Judicial Commissioners should have held that the assessee firm was not entitled to deduct the above two items as items of expenditure.

(*e*) That the Judicial Commissioners should have held that the case under reference did not fall under Section 10 (2) (iii), Income Tax Act.

The grounds affect the respondents only and not assessees in general. Reliance has however been placed on the following observations made by us in our judgment, which are said to affect assessees in general: "It is also not possible to draw any distinction between capital borrowed and capital contributed. It is only a different way of expressing one and the same thing. Capital contributed by a capitalist partner is capital borrowed from him by the firm'.

It is perhaps on these observations that grounds (*c*) and (*d*) in the memorandum for leave are based. But these observations, must be read along with the preceding paragraph; and that paragraph makes it abundantly clear that if the conditions of Section 10, Clause (2) (iii) are complied with nothing turns upon the use of the expression "money contributed by a partner" as opposed to the expression "money borrowed from a partner." Another ground urged by the learned advocate for the appellant in the course of his arguments is that Section 10, Clause (2) (iii) refers to capital borrowed from a stranger and not from a partner and that the decision of this Court is therefore wrong. But no such distinction was made either in the reference under Section 66, Clause (2) nor has any such ground been raised in the memorandum for leave to appeal to His Majesty in Council, and cannot therefore be considered.

Apart from what is said above it is sufficient to observe that Section 10, Clause (2), sub-Clause (iii) makes a distinct departure from the English law which provides that interest on capital employed in the business is not an allowable deduction: see

Halsbury Vol. XVII, para. 332. If in enacting the present section the legislature intended that interest paid to a partner on capital borrowed from him should not be an allowable deduction from the profits earned, it should have said so. The learned advocate for the applicant has invited our attention to the case, Application No. 16 of 1932, *Commissioner of Income Tax* v. *Bulchand Keshavadas.* But that case is clearly distinguishable. In that case the Income Tax Commissioner had declined to refer the case to us and he was compelled to do so. He was anxious to have a decision on the point whether we had jurisdiction to compel him to refer a case when he thought that no question of law was involved in it. That was a question of general importance and not limited to the circumstances of that particular case only. On behalf of the respondents our attention has been invited to the case of *Raja Rajeswara Sethupathi* v. *Tiruneelakantam Servai.* In that case a Full Bench of the Madras High Court consisting of Schwabe, C. J., and Coutts Trotter and Kumaraswami Sastri, JJ., refused to grant leave under Section 109, Clause (c), Civil Procedure Code, on the ground that it would not be right to call upon a party whose financial interest in the matter is small to incur the expense of supporting the judgment of the High Court before their Lordships of the Privy Council. At p. 233, (of A.I.R. 1923 Mad.) SCHWABE, C.J., has said :

'In similar cases on applications for special leave to appeal made to their Lordships of the Privy Council, a condition has been imposed upon the appellant that, whatever be the result of the appeal, he should pay the costs of the other party as between solicitor and client. See *Spooner* v. *Juddow, Shibnarain Ghose,* In re, and *Indian Irrigation Trust Board of Natal* v. *Govindaswami.* I think that this is a proper case for such an order if it is a matter upon which I am entitled to express an opinion. The question has been raised before us whether we have power to impose such a condition. In *Clark* v. *Brajendrakishore* JENKINS, C.J. and CASPERSZ, J. held that no such power existed in the Indian Courts but was confined to the Privy Council. There sult of such finding is curious... What is the duty of the Court if it thinks that the case is a fit one for consideration by His Majesty in Council but that it would not be right to call upon one party whose financial interest in the matter is small, to incur the risk of the costs of the appeal. Assuming the decision in *Clarke* v. *Brajendrakishore* is right, and in my judgment in view of the fact that that case went before the Privy Council and special leave to appeal was granted and it was not then

suggested that the Calcutta High Court could have itself imposed any condition, it is not possible for this Court to hold otherwise, the only course open to us is to refuse leave and to leave the appellant if so advised, to apply to the Privy Council for special leave.'

It appears that in that case no leave was applied for before their Lordships of the Privy Council and the question whether High Courts in India are competent to impose a condition as to costs therefore remains where it was. An authoritative decision upon that point is more necessary under Section 60-A, Income-tax Act. Under that section, it is only a question of law which may be referred to the Court. As the Income-tax Commissioner is a party to the proceedings in 9 cases out of 10 a decision given against him becomes a decision of importance as between him on the one hand and assessees in general on the other. The pecuniary amount involved in most of these cases is small and it is difficult for the assessee concerned in a particular case to incur the expense of appearing before their Lordships of the Privy Council. As we have taken the view that the points raised by the learned Commissioner are not points of general importance, it is not necessary for us to consider whether it is competent for us to refuse leave on the grounds mentioned in *Rajarajeswara Sethupathi* v. *Tiruneelakanta Servai.* But we hope that the legislature will consider the advisability of conferring a power upon the High Court to impose a condition in a fit case, at the time of granting leave to appeal to the Privy Council (at any rate in cases falling under Section 65 A (2) Income-tax Act) that whatever may be the result of the appeal, the appellant should pay the costs of the other party as between solicitor and client. We accordingly dismiss this application.

[IN THE BOMBAY HIGH COURT]

COMMISSIONER OF INCOME TAX, BOMBAY

v.

ABUBAKER ABDUL RAHMAN.

SIR F. W. BEAUMONT, C.J., & BLACKWELL, J.

October 16, 1935.

INCOME TAX—ACCOUNTING PERIOD—ASSESSEE KEEPING DIFFERENT ACCOUNTING PERIODS FOR INDIVIDUAL BUSINESS AND FIRM—SHARE IN FIRM ASCERTAINED AFTER TERMINATION OF ACCOUNTING PERIOD OF INDIVIDUAL BUSINESS—SHARE OF PROFITS OF FIRM, WHETHER CAN BE TREATED AS HAVING ESCAPED

ASSESSMENT FOR PURPOSES OF SUPER TAX—PROPER TIME FOR ASSESSMENT—INDIAN INCOME TAX ACT (XI OF 1922), SECTIONS 2 (11), 14, 16, 22 (2) AND 55.

Under the Indian Income-Tax Act the tax payable in a particular year is not charged on the income of that year, but on the income of the previous year.

Where an assessee has two businesses with different accounting periods, he cannot fix two different dates which will give him two separate previous years for the purpose of the Income tax Act; but he can fix one date for himself, and a firm of which he is a member may fix another date, and if the date which the assessee has fixed for himself is earlier than the date which the firm has fixed, the assessee cannot be compelled to include in the return of his total income his share in the profits of the firm, which were ascertained after the expiry of the accounting period which the assessee has fixed for himself. Nor can his share in the profits of the firm, when it is ascertained, be treated as having escaped assessment in the previous year for the purposes of levying super tax on the assessee.

The assessee made up his accounts up to November 9, 1931. A firm of which he was a partner made up its accounts up to December 31, 1931. In the year of assessment ending March 31, 1933 the assessee was assessed on the income of Rs. 26,262 nothing being included in respect of his share in the profits of the firm. The share of the assessee in the profits of the firm was assessed at Rs. 1,14,812 on December 31, 1931. The Income-tax Officer contended that this sum had escaped assessment within the meaning of Section 34 for purposes of levying euper tax under Section 55: Held, *that the assessee was only liable to income-tax as well as super tax in respect of the Income of the previous year which ended on November 9, 1931, and the profits to which he was entitled at the date of the assessment of the firm, that is, on December 31,1931 could be assessed only in the next year,* i.e., *November 10,1931, to November 9, 1932.*

Cases referred to :

BEHARI LAL MULLICK, *In re* [1927] (I.L.R. 54 Cal. 630; 31 C.W.N. 557; 103 I.C. 609; A.I.R. 1927 Cal. 543).

COMMISSIONER OF INCOME-TAX *v.* TEHRI GHARWAL STATE [1934] (2 I.T.R. 1; 61 I.A. 1; A.I.R. 1934 P.C. 34).

Reference made by the Commissioner of Income-tax, Bombay Presidency and Aden. Civil Ref. No. 5 of 1935.

K. Mc I Kemp and *G. Louis Walker* for Petitioner.
F. J. Coltman and *Jamshed Kanga* for Opposite Party.

BEAUMONT, C.J.—This is a reference under Section 66 (2), Income Tax Act, 1922, in which the Commissioner raises this question :—

'In view of the provisions of Section 16 read with Section 14 (b) of the Act has the Income Tax Officer correctly included in the computation under Section 16 of the Act, of the total income of the assessee for the purposes of his 1932-33 assessment, his share of Rs. 1,14,812 in the income of the Imperial Movietone Co., for the calendar year 1931'.

The reason for raising that question requires some explanation.

The assessee is a gentleman named Abubaker Abdul Rahman, and the year of assessment is the year 1932-33, that is the year ending 31st March, 1933. The assessee is a partner in two different firms, one, Abubaker Abdul Rahman & Co., and the other the Imperial Movietone Co. He also has certain property which produces income, apart from his interest in the firms. The accounts of the assessee and of the firm of Abubaker Abdul Rahman & Co., are made up to Diwali, that is, in the case of the previous year in respect of the year of the assessment, 9th November 1931. But the Imperial Movietone Co., makes up its accounts to 31st December.

That firm was only started on 1st January 1931, so that, it is the first accounting period which ends on 31st December, 1931. In the return of the assessee for income tax purposes he included his property received from outside sources, and deducted a loss in respect of the firm of Abubaker Abdul Rahman & Co., and he was assessed on 3rd February 1933 on an income of Rs. 26,262, nothing being included in that income in respect of any profits of the Imperial Movietone Co. The accounts of that Company were made up to 31st December 1931, and the share of the assessee in the profits of that firm was assessed at Rs. 1,14,812. The Income Tax Officer contended that that sum had escaped assessment within Section 34. Income tax had been paid direct by the Imperial Movietone Co., and therefore no income tax was payable by the assessee on his share of the profits, having regard to Section 14 (2) (*b*) of the Act. But the Income Tax Officer was of opinion that that income had escaped assessment, and was liable for super-tax under Section 55 of the Act, and his decision was upheld on appeal by the

Assistant Commissioner. The assessee, on the other hand, contends that the income which he received as a member of the Imperial Movietone Co., was received by him after the year for which he was assessed, and that those profits will have to be brought into the next year of assessment and have not escaped assessment.

The question involves a consideration of certain sections of the Income-tax Act. In the first place, it is necessary to notice that according to the decision of the Calcutta High Court in *Behari Lal Mullick In re*, the tax payable in the current year is not charged on the income of that year, but on the income of the previous year, that is to say, the tax under the Indian Act is actually levied on the income of the previous year and not as in England levied on the income of the current year though that income may be, and often is, estimated by reference to the income of the previous year, since in England the return has to be made before the current year has expired. That decision of the Calcutta High Court was apparently approved by the Privy Council in *Commissioner of Income-tax* v. *Tehri Garhwal State* though whether the full implications of the doctrine are realised by the income-tax authorities in India may be doubted. If that is the basis on which income-tax is levied, it is obviously of great importance to ascertain what the "previous year" is; and "previous year" is defined by Section 2 (11), Income Tax Act, in these terms:—

"Previous year" means—

(a) the 12 months ending on 31st day of March next preceding the year for which the assessment is to be made, or, if the accounts of the assessee have been made up to a date within the said 12 months in repect of a year ending on any date other than the said 31st day of March, then at the option of the assessee the year ending on the day to which his accounts have so been made up:"

Then there is a proviso that the assessee is not to be entitled to change the meaning of the expression "previous year" when once fixed by him, without the consent of the Income Tax Officer. There is, I think, nothing in that definition to suggest that an assessee can fix more than one date which determines the previous year. If an assessee has two businesses with different accounting periods for those two businesses, he cannot, I think, fix two different dates, which will give him two separate previous years for the purpose of the Income-tax Act. But on the other hand, I can see no reason why an assessee should not fix one date for

himself, whilst a firm of which he is a member with others fixes another date. " Assessee " is defined in sub-section (2), Section 2, as meaning a person by whom income tax is payable and under Section 3 income tax is charged not only on every individual but on every Hindu undivided family, company, firm and other association of individuals. So that, in my opinion a firm is clearly an assessable unit and therefore an assessee under the Income tax Act. The position which arises in this case is that the assessee has fixed for himself as the " previous year " the year ending 9th November 1931, whilst the Imperial Movietone Company in which the assessee is a member, has fixed as the "previous year" the year ending 31st December 1931.

The next section to look at is Section 22 (2) which provides that in the case of any person other than a company, falling within the provisions of that section, a return has to be made setting forth the total income during the previous year. That Section applies both to the assessee and to the Imperial Movietone Company which is also an assessee. For the purpose of making a return as to his total income, the assessee has to comply with Section 16 the effect of which read with sub-section (2), Section 14, is that he has to include in his total income such an amount of the profits or gains of any firm which have been assessed to income tax as is proportionate to his share in the firm at the time of such assessment. What Section 14 (2) provides is that income tax is not payable by an assessee in respect of his share in the profits of a firm, which has been already assessed, because naturally that share cannot be taxed twice over. If the firm is assessed, and pays the tax, then the individual members of that firm are not separately assessable in respect of their shares in the profits. But when it comes to a return of the total income of the partners for the purpose of super tax then, they have to include in their total income their respective shares in the profits of the firm, which have been separately assessed.

Now the position of the assessee in this case is that he has to make a return of his total income down to 9th November 1931. It is quite clear that he cannot in that return include income which is proportionate to his share in the profits of the Imperial Movietone Company at the time of the assessment of these profits, since that share can only be ascertained after the accounting period ending on 31st December 1931. Therefore it seems to me clear that the assessee in respect of the previous year, which

applies to him, cannot be required to include his share of profits in the Imperial Movietone Company. That is not really questioned by the income tax authorities. But they contend that as soon as the share of the profits of the assessee in the Imperial Movietone Company was ascertained, then that share was liable to tax, and must be treated as having escaped assessment under Section 34. I cannot agree with that view of the matter. It seems to me that that would really involve that the assessee was accountable in respect of two previous years, one ending 9th November and the other ending—so far as his position as a member of the Imperial Movietone Company was concerned—31st December and that I think is wrong. I think the assessee is only liable to tax in respect of the previous year which ends on 9th November 1931, and that any profits to which he was entitled from the Imperial Movietone Company at the date of the assessment of that company must necessarily fall within the next year of assessment of the assessee —the year, that is, from 10th November 1931 to 9th November 1932. Section 55, which imposes super tax which is the tax which the Commissioner seeks to levy in this case, does not I think carry the question any further, because all that that section provides is that in addition to the income tax charged for any year, there shall be charged, levied and paid for that year in respect of the total income of the previous year, an additional duty of income tax (in this Act referred to as super tax).

The language of that section, so far as is material, is identical with the language of Section 3 and appears therefore according to the decision of the Calcutta High Court in *Behari Lal Mullick, In re*, to make the income chargeable to super tax as well as to income tax, the income of the previous year. As I have already said, in the income of the previous year, the assessee is not bound to include something to which he became entitled after the termination of that year. For those reasons, I think that the question propounded by the learned Commissioner must be answered in the negative. Costs to be paid to the assessee, to be taxed on the Original Side scale.

BLACKWELL, J.—I agree and have nothing to add.

Reference answered accordingly.

[IN THE PRIVY COUNCIL].

COMMISSIONER OF INCOME TAX, BENGAL

v.

MERCANTILE BANK OF INDIA & OTHERS.

LORD THANKERTON, LORD RUSSEL OF KILLOWEN, LORD MAUGHAM, SIR SIDNEY ROWLATT and SIR SHADI LAL.

May 20, 1936.

INCOME TAX—COMPANY—ACCUMULATED PROFITS—DISTRIBUTION AS BONUS DEBENTURES—ASSESSABILITY—'INCOME,' MEANING OF—MOTIVE OF SHAREHOLDERS, HOW FAR MATERIAL—INDIAN INCOME TAX ACT (XI OF 1922), Section 4.

Sir David Yule died leaving a large estate which mainly consisted of holdings of shares in certain companies. All the ordinary share capital in some of these companies was wholly held by the trustees of his estate in their own name or through nominees. In some of the companies there were also other shareholders. The companies had large accumulations of undistributed profits and, as they had to meet some heavy outstandings, the trustees devised a scheme to make the accumulated profits available for the purpose of meeting such charges. The accumulated profits were issued as bonus debentures in the names of the trustees in the first graup of companies. Preferred ordinary shares were issued to the trustees alone in the second group of companies, and debentures were issued to the trustees in respect of the preferred ordinary shares. The debentures were subsequently redeemed. The question being whether the trustees could be assessed to income-tax in respect of the bonus debentures issued to them: Held, *affirming the decision of the High Court of Calcutta, that, by this transaction no income, profits or gains accrued or arose or was received by the trustees within the meaning of Section 4 of the Indian Income-tax Act and the trustees were not liable to be assessed to income-tax in respect of the debentures. Held further that the personal motive, or purpose of the individual shareholders, even though they held a controlling interest in the company was irrelevant as the company had in fact capitalised the accumulated profits.*

Inland Revenue Commissioners v. *Blott (1921) A.C. 171 and Commissioners of Inland Revenue* v. *Fischer's Executors (1926 A.C. 395)* followed.

Swan Brewery Co. v. *Rex. (1914 A.C. 231)* distinguished.

INCOME TAX COMMISSIONER *v.* SHAW WALLACE & Co. (136

I.C. 742; 59 I.A. 206; A.I.R. [1932] P.C. 138; [1932] Comp. Cas. 276).

LONDON COUNTY COUNCIL *v.* ATTORNEY-GENERAL (1901 A.C. 26) referred to.

Appeal from a judgment of the Calcutta High Court reported as [1935 I.T.R. 163].

A.M. Dunne, K.C., Gavin Simmonds, K.C., and *R.P. Hills* for the appellant.

A.M. Latter, K.C., L.P.E. Pugh and *J.P. Lindon* for the respondent.

LORD THANKERTON.—This is an appeal from a judgment of the High Court of Judicature at Fort William in Bengal, delivered on a reference of questions of law by the Commissioner of Income tax, Bengal, under Section 66 (1) of the Indian Income Tax Act, [1922] (XI of 1922).

These questions of law arose in course of an assessment for super tax and surcharge made by the Income tax Officer upon the respondents, as trustees of the late Sir David Yule, for the year ending March 31, 1932, in respect of Rs. 5,71,30,000 being the nominal amount of certain bonus debentures issued to them in respect of their shareholding in certain companies in the year ending March 31, 1931. The respondents appealed to the Assistant Commissioner, Calcutta, and while the appeal was pending, the Commissioner, of his own motion, made the present reference to the High Court, asking the following questions of law, *viz.*,

" *First Question.*—The assessee being in his own name and through nominees the holder (a) of the whole of the share capital of companies as specified in the case, and (b) together with two trustees in their individual capacity, of the whole of the share capital of one company as specified: these companies being investment companies of the nature described in the case: and the said companies having issued to the assessee by way of bonus, debentures which have subsequently been paid off through the transaction specified in the case....................(*quaere*) was there by these transactions any income, profits or gains which accrued or arose to or were received by the assessee, within the meaning of Section 4 of the Act ? "

" *Second Question.*—If any such income did arise, when did it so arise ? "

"*Third Question.*—If any such income did arise was its quantum an amount corresponding (a) to the full amount of the

debentures or (b) to such part only as derived from the received and accumulated revenue profits of the companies, and excluding such part as derived from appreciated valuations of the companies' investment holdings ? "

" FOURTH QUESTION.—In the latter alternative, on what principles are the respective quanta to be accounted and ascertained "

The parties were agreed in asking for the decision of the Board on the first question only. The facts are fully set forth in the statement of the case by the Commissioner, but they may be summarised as follows : The late Sir David Yule died on July 3, 1928, leaving a very large estate, which mainly consisted of holdings of shares in 30 companies with 20 of which the present appeal is concerned, being the companies which issued the debentures in question. The Commissioner has divided these 20 companies into two groups ; in the first group all the capital was ordinary share capital, wholly held by the trustees in their own name or through nominees, the trustees being the beneficial owners of all the shares, and the debentures were issued wholly in the name of the trustees. In the second group, the trustees and their nominees did not hold all the ordinary share capital, the other shares being held by others of the 30 companies, and in one case, that of the Calcutta Discount Company, certain shares were held by two of the trustees individually. In the case of each company in the second group an issue of preferred ordinary shares was made to the trustees alone, and the debentures in question were thereafter issued to the trustees in respect of the holding of preferred ordinary shares.

For the purposes of the argument before their Lordships no distinction was drawn between the two groups of companies as regards the procedure under which the debentures came to be issued, and the procedure of the Calcutta Discount Company, Limited, was taken as sufficiently typical of the procedure of all the companies for that purpose.

The following is an extract from a special resolution of that company passed on January 3, 1930 and confirmed on January 22, 1930 :—

" 2. That the capital of the company be increased by the creation of 725 preferred ordinary shares of Rs. 100 each, and the same be issued to such persons as the secretaries may think fit.

(*a*) The preferred ordinary shares shall rank in priority to the ordinary shares both as to dividend and re-payment of capital, and shall carry the right to a non-cumulative dividend of such amount as may be declared by the company in general meeting, but so that the ordinary shares shall not be entitled to any dividend in any year unless and until at least 5 per cent. has been declared on the preferred ordinary shares for that year. The said preferred ordinary shares shall have no further right to participate in profits or surplus assets in a winding-up."

"(*b*) The date from which such shares shall rank for dividend shall be the 1st day of January 1930, or such later date as the secretaries shall think fit."

Of these 725 preferred ordinary shares, 629 were allotted to the respondents, as trustees of the estate of the late Sir David Yule, and the residue (96) partly to one trustee and partly to another.

At the same time the Calcutta Discount Company, Limited, adopted a new Article as article 126 of its articles of association, from which the following is an extract:—

"126. The company in general meeting may at any time and from time to time pass a resolution that any sum not required for the payment or provision of any fixed preferential dividend and (*a*) for the time being standing to the credit of any reserve fund or reserve account of the company, including premiums received on the issue of any shares, debentures or debenture stock of the company, or (*b*) being undivided net profits in the hands of the company, be capitalised, and that such sum be set free for distribution, and be appropriated as capital to and amongst the preferred ordinary shareholders and ordinary shareholders respectively in the proportions in which they would have been entitled thereto if the same had been surplus distributable profits, and in such manner as the resolution may direct and such resolution shall be effective; and the secretaries shall, in accordance with such resolution, apply such sum in paying up in full any unissued shares in the capital or any debentures or debenture stock of the company on behalf of the shareholders concerned, and appropriate such shares, debentures or debenture stock, and distribute the same credited as fully paid-up amongst such shareholders in the proportions aforesaid in satisfaction of their shares and interests in the said capitalised sum, or shall apply such sum or any part thereof on behalf of the shareholders aforesaid in paying up the whole or part of any uncalled balance which shall for the time being be unpaid in respect of any issued shares of any of the said

classes held by such shareholders or otherwise deal with such sums as directed by such resolution."

The following is an extract from minutes dated March 14, 1931:—

"CALCUTTA DISCOUNT COMPANY, LTD."

"Minutes of the Secretaries, dated March 14, 1931."

"The Secretaries having taken into consideration the financial position of the company and being satisfied that such position justified the distribution from the reserve fund of Rs. 1,45,00,000 in the form of a special capital bonus free of income tax it was decided to recommend to the shareholders the payment of such a special capital bonus to be satisfied by the distribution among the members holding preferred ordinary shares in the company on March 24, 1931, of Rs. 1,45,00,000 of debentures carrying interest at 3 per cent. per annum from the first day of January 1931, in proportion to the number of preferred ordinary shares respectively held by such members.

"The notice convening the requisite meeting having been prepared it was decided to issue the same to the shareholders.

"Andrew Yule & Co., Ltd.
"(Sd.) J. SIME,
"Managing Director,
"Secretaries."

At an extraordinary meeting of the Calcutta Discount Company held on March 24, 1931, the following resolutions were passed:—

"(1) That it is desirable to capitalise a sum of Rs. 1,45,00,000 being part of the amount standing to the credit of the reserve fund and accordingly that a special capital bonus of Rs. 1,45,00,000 free of income-tax be declared and such capital bonus be applied on behalf of the persons who on the 24th day of March 1931, were the holders of the 725 issued preferred ordinary shares of the company in payment in full for Rs. 1,45,00,000 of debentures of the company carrying interest at 3 per cent. per annum from the first day of January 1931 (and to be charged upon the whole undertaking of the company).

"(2) That to the above resolution the Secretaries be and they are hereby authorised to create and issue such debentures as a special capital bonus free of income tax credited as fully paid and to distribute the same to the holders registered on the 24th day of

March 1931, of the 725 preferred ordinary shares in the company's capital in proportion to the number of such shares held by them respectively in full satisfaction of such capital bonus as aforesaid."

The following is an extract from the minutes:—

"CALCUTTA DISCOUNT COMPANY, LTD."

"Minutes of the Secretaries, dated March 25, 1931."

"The resolution passed at the extraordinary general meeting of the company held on the 24th day of March 1931, that it was desirable to capitalise Rs. 1,45,00,000 being part of the company's reserve fund having been considered and it was decided to create and issue a series of debentures of a total nominal value of Rs. 1,45,00,000 consisting of 28 debentures of Rs. 5,00,000 each, one debenture of Rs. 4,00,000 and five debentures of Rs. 20,000 each all carrying interest at the rate of 3 per cent. per annum and to distribute the same to the holders registered on the 24th day of March, 1931, of the 725 issued preferred ordinary shares in proportion to the number of such shares held by them respectively in full satisfaction of the capital bonus. One debenture for Rs. 5,00,000 was thereupon sealed and directed to be registered with the Registrar of joint stock companies and that on obtaining the Registrar's certificate the remaining debentures be sealed and issued."

As a result of the foregoing proceedings debentures of the Calcutta Discount Company to the amount of Rs. 1,25,80,000 were issued to the respondents, the residue of the issue being allotted severally to the two trustees who each held a small quantity of the preferred ordinary shares.

The debentures are dated March 24, 1931, and the amounts secured were repayable at latest on December 31, 1940, and were repayable at the option of the Company at any time after three months' notice.

The circumstances under which these debentures came to be issued are conveniently summarised in the judgment of the High Court as follows:

"All the companies had very large accumulation of undistributed profits. The actual figures are immaterial. The trustees had to meet very heavy outgoings for duties both in the United Kingdom and in India in relation to the estate of the deceased, and it was to provide funds for such duties that a scheme was devised whereby accumulated profits would come into their hands and be available for the purpose of meeting such charges."

In fact the debentures were all redeemed by the companies at various dates prior to the end of February, 1933, but the crucial date in the present question is the date of the issue of the debentures.

The High Court decided against the claim of the Crown, holding that the case was governed by the principles laid down by the House of Lords in the cases of *Inland Revenue Commissioners* v. *Blott* and *Commissioners of Inland Revenue* v. *Fisher's Executors*. They rejected an argument of the Advocate-General directed against the validity of the proceedings of the companies, upon the ground that it was not open on the case as stated by the Commissioner, which proceeds on the footing that the transactions of the companies are unimpeachable. This argument was not pressed at the hearing before their Lordships.

The question being whether, by the transactions in question, any income, profits or gains accrued or arose to or were received by the assessees within the meaning of Section 4 of the Indian Income Tax Act, the Crown maintained (first) that the decisions in the cases of *Blott* and *Fisher* (*supra*), which were under the Imperial Income Tax Act, were not applicable, and that the decision of this Board in *Swan Brewery Company, Ltd.* v. *Rex* applied in the present case, and (second) that, in any event, the facts in the present case rendered it distinguishable from the cases of *Blott* and *Fisher* in respect that the purpose of the transactions in the present case was not a genuine company purpose, but for the individual benefit of the controlling shareholders.

In the first place, their Lordships are of opinion, that, as regards the point here in issue, there is no ground for distinction between the Imperial Act and the Indian Act. In *Income Tax Commissioner* v. *Shaw Wallace & Co.*, Sir George Lowndes, in delivering the judgment of the Board, while expressing a general warning against treating questions under these Acts as *in pari materia*, said, "The object of the Indian Act is to tax, "income," a term which it does not define. It is expanded, no doubt, into "income, profits and gains but the expansion is more a matter of words than of substance." This states compendiously the same view as expressed in regard to the Imperial Act by LORD MACNAGHTEN in *London County Council* v. *Attorney-General*.

In the case of the *Swan Brewery Company* the company had passed resolutions by which its capital was increased by a new

issue of shares, and a portion of the accumulated profits standing to the credit of the reserve fund corresponding to the amount payable on allotment of the shares was transferred to the credit of the share capital account, the new shares being then allotted as fully paid among the shareholders *pro rata*. It was held by the Board that these transactions were in effect a declaration of a dividend within the meaning of the Dividend Duties Act, 1902, of Western Australia, under Section 2 of which the word "dividend" was defined as including "every profit, advantage or gain intended to be paid or credited or distributed among the members of any company." In delivering the judgment of the Board, LORD SUMNER, referring to the argument of the appellant company, said :

"The duty claimed is not, it is said, a duty on or in proportion to any advantage either to the company or the shareholder measured by the increased stability of the company's own position or the increased facility to the shareholder in marketing his shares ; it is measured by and is levied upon the whole nominal value of the new shares allotted, which is not the same thing as the value of the advantage distributed. Is this argument sound? Their Lordships agree with the Supreme Court of Western Australia in thinking that it is not. There can be no doubt that the new shares were distributed and were not the same things as the old ones. They certainly were supposed to be advantages to the members of the company, none the less that the making of the issue was probably an advantage to the company also. In so flourishing a business doubtless they really were advantages. The new shares were credited as fully paid, and, what is more, they were fully paid, for after the allotment the company held £ 101,450 as capital produced by the issue of those share and for that consideration, and no longer as an undivided part of its accumulated reserve fund. True, that in a sense it was all one transaction, but that is an ambiguous expression. In business, as in contemplation of law, there were two transactions, the creation and issue of new shares on the company's part, and on the allottees' part the satisfaction of the liability to pay for them by acquiescing in such a transfer from reserve to share capital as put an end to any participation in the sum of £ 101,450 in right of the old shares, and created instead a right of general participation in the company's profits and assets in right of the new shares, without any further liability to make a cash contribution in respect of them. In the words of PARKER, C. J., 'Had the company distributed the £ 101,450 among the shareholders and had the shareholders repaid such sums to the

company as the price of the 81,160 new shares, the duty on the £101,450 would clearly have been payable. Is not this virtually the effect of what was actually done? I think it is."

It is unnecessary to resume in detail the facts in the cases of *Blott* and *Fisher*. In *Blott's Case* the company applied accumulated profits in satisfaction of the amount due on the issue of bonus shares, while in *Fisher's Case* accumulated profits were similarly applied in respect of bonus debentures. In the latter case LORD CAVE (at p. 400) states the principle of the decision in *Blott's Case*, by quoting the opinion of LORD HALDANE in that case, which was as follows:

"My Lords, for the reasons I have given I think that it is, as matter of principle, within the power of an ordinary joint stock company with articles such as those in the case before us to determine conclusively against the whole world whether it will withhold profits it has accumulated from distribution to its shareholders as income, and as an alternative not distribute them at all, but apply them in paying up the capital sums which shareholders electing to take up unissued shares would otherwise have to contribute. If this is done, the money so applied is capital and never becomes profits in the hands of the shareholder at all. What the latter gets is no doubt a valuable thing. But it is a thing in the nature of an extra share certificate in the company."

The case of bonus debentures was held to be indistinguishable from that of bonus shares. Nor does it seem possible to distinguish the facts of the present case from those in *Fisher's Case* apart from the contention of the Crown that the real purpose of the transactions in the present case forms a relevant ground of distinction.

The case of the *Swan Brewery Company* was referred to in certain of the opinions in *Blott's Case*. LORD HALDANE (at p. 188) says:—

"There the transaction was in many respects analogous to that here. But the taxing statute was couched in very different language. There were expressions in the judgment which may be construed as having gone rather further, and treated the payment made by the company as equivalent in substance to a payment by the company to the shareholders, and by them back to the company. It may have been so, and without a fuller knowledge of the facts in the case and of the local law than the report discloses, it is difficult to be quite sure about the point, but what is clear is that

the wide character of the word 'advantages' was a primary consideration in what was said by their Lordships who took part in advising His Majesty. I therefore, do not feel embarrassed by the decision in that case."

Lord Finlay (at p. 199) thought that the reasoning in the *Swan Brewery Company* case was inconsistent with the decision of the House of Lords in *Bouch* v. *Sproule*. Lord Cave (at p. 202) said that the decision in the *Swan Brewery Company case* was no doubt fully supported by the definition clause in the Western Australia Act, but that, otherwise, he would hold it to be inconsistent with *Bouch* v. *Sproule*. Lord Dunedin, who dissented in *Blott's case* stated (at p. 203) that the *Swan Brewery Company case* was a decision upon an Australian statute in the words of which if anything became an " advantage " it would fall within the tax. Lord Sumner, who also dissented in *Blott's case*, and also delivered the judgment of the Board in the *Swan Brewery Company case*, was clearly of opinion (at p. 217) that what was said by the Judicial Committee in the latter case as to the effect in law and in business of a distribution of bonus shares, was part of the decision and could not be distinguished from *Blott's case*.

Having carefully considered the judgment in the *Swan Brewery Company case* and the varying views taken of it in *Blott's case*, their Lordships are of opinion, that the judgment must be regarded as having been primarily based on the distribution of the new shares being advantages within the meaning of the particular Act under consideration, while the further expression of opinion in the judgment rather regarded the transaction as involving, in substance, a distribution of accumulated profits among the shareholders and a repayment by them to the company, although the operation was in fact short circuited. For the purpose of the present question, their Lordships are clearly of opinion, that the decisions under the Imperial Income Tax Act are more relevant to the similar question under the Indian Income Tax Act, than a decision under the different terminology of the Western Australian Act.

Lastly, their Lordships are clearly of opinion, that the personal motive or purpose of the individual shareholders, even if they hold a controlling interest in the company, is irrelevant, if it is made out that the company has in fact capitalised the accumulated profits. It is sufficient to quote from the opinion of Lord Sumner in *Fisher's case* in the decision of which he concurred, as follows (at p. 411) :—

"In any case desires and intentions are things of which a company is incapable. These are the mental operations of its share-holders and officers. The only intention that the company has is such as is expressed in or necessarily follows from its proceedings. It is hardly a paradox to say that the form of a company's resolutions and instruments is their substance. At any rate in the present case, there is no need to distinguish between form and substance in the transaction itself or to refer to desires or intentions, further than to examine what was done, for everything was carried out in plain terms and without concealment. What the requisite majorities of the share-holders desired and intended is pretty plain, too, but that is another mater."

Their Lordships are, therefore, of opinion that the first question of law referred by the Commissioner of Income tax should be answered in the negative, that the Judgment of the High Court should be affirmed, and that the appeal should be dismissed with costs. They will humbly advise His Majesty accordingly.

Appeal dismissed.

Solicitor for the Appellant :—*The Solicitor, India Office.*
Solicitors for the Respondent :—*Nye, Moreton & Calwes.*

[IN THE HIGH COURT OF LAHORE.]

LALLA MAL SAMGHAM LAL
v.
COMMISSIONER OF INCOME TAX, PUNJAB.

SIR DOUGLAS YOUNG, C. J., COLDSTREAM, MONROE, SKEMP, BHIDE, CURRIE, ABDUL RASHID, JJ.

April 30, 1936.

PROPERTY—'ANNUAL VALUE'—MUNICIPAL TAX PAYABLE BY TENANT—WHETHER PORTION OF ANNUAL VALUE—AMOUNT PAYABLE BY TENANT, WHETHER CONCLUSIVE EVIDENCE OF ANNUAL VALUE—INDIAN INCOME TAX ACT (XI OF 1922), SEC. 9, (1) AND (2).

Held, by the Full Bench (SIR DOUGLAS YOUNG, C. J., COLDSTREAM, MUNROE, SKEMP, CURRIE, BHIDE AND ABDUL RASHID, JJ.) :—*In estimating the sum for which a property might reasonably be expected to let from year to year, for the purpose of assessing the owner of such property to income-tax under Sec. 9 of the Indian Income Tax Act the amount paid by the tenant on account of municipal house tax should be included, that is, should be treated as part of the rent payable by the tenant to the landlord. The term 'annual value' does not necessarily mean the annual money benefit derivable from the property by the landlord.*

The amount of rent payable by the tenant to the landlord is, however, only prima facie *evidence of annual value and a consideration of the rents paid for similar and similarly situated properties in the locality may show the 'annual value' in any particular instance to be less or more than the rent actually paid.*

CHUNNAMAL SALIGRAM *v.* COMMISSIONER OF INCOME TAX, PUNJAB [1931] (131 I.C. 193; A.I.R. 1931 Lah. 320; 5 I.T.C. 316) *overruled.*

KRISHNA LAL SEAL, IN RE [1932] (I.L.R. 60 Cal. 357; 140 I.C. 1; A.I.R. 1932 Cal. 886; 6 I.T.C. 293) *followed.*

Case stated by the Commissioner of Income Tax, Punjab, N.W.F.P., and Delhi under Section 66 (2) of the Indian Income Tax Act, in the matter of assessment of Messrs. Lalla Mal-Samgham Lal of Delhi for the year 1934-1935.

Nawal Kishore, for the assessees.

J. N. Aggarwal, for the Commissioner of Income Tax. The necessary facts are stated in the judgment.

The case came on for hearing before ADDISON and ABDUL RASHID, JJ., who made the following

ORDER OF REFERENCE TO A FULL BENCH :—

" Under Section 66 (2) of the Indian Income-tax Act the Commissioner of Income-tax, Punjab, has referred the following two questions of law to this court, namely :—

(1) Whether the enhancement of income from the property from Rs. 50,088 to Rs. 51,802 by the Assistant Commissioner is legal ?

(2) Whether the house-tax paid by the tenants of the petitioner on account of Delhi Municipal house tax is to be included to arrive at " the annual value " ?

As the two questions are inter-dependent and as the Commissioner has asked that the second question should be referred to a Full Bench in view of conflict of authority we have come to the conclusion that this case should be referred to a Full Bench with the permission of the Honourable Chief Justice.

The second question has already been before a Full Bench of this Court. See *Chunnamal Saligram* v. *Commissioner of Income-Tax, Punjab.* I was member of that Bench. I was inclined to hold that the question was one more or less of fact but, if it was to be considered a question of law, it should be answered in the affirmative. Three Judges, namely TEK CHAND, JAI LAL and AGHA HAIDER, JJ., were of the view that it should be answered in the negative, while DALIP SINGH, J., was of opinion that the question was one of fact. The question was, therefore, answered in the negative on the view taken by the majority of three Judges to two.

The same question came before a Full Bench of three Judges, including the Honourable Chief Justice of the Calcutta High Court shortly afterwards : See *Krishna Lal Seal, In re.* This Bench dissented from the decision of this Court, the princi-

pal portion of the Judgment being set out in the order of the Commissioner stating this case. It is on account of this divergence of opinion that the Commissioner has asked that it should be referred again to a Full Bench of this Court. I still hold the same view as I took in the former Full Bench of this Court, namely, that the answer to the second question should be in the affirmative. My learned brother agrees that this is a fit case again to be referred to a Full Bench.

For these reasons we would refer the two questions to a Full Bench if the Chief Justice agrees."

The case was thereupon heard by a Full Bench of seven Judges.

Lala Badri Das, Nawal Kishore and *R. K. Tandon,* for the Assessee.

J. N. Aggarwal, S. M. Sikri and *M. Aslam Khan,* for the Commissioner of Income Tax.

ORDER OF THE HIGH COURT.

This is a reference by the Commissioner of Income Tax under Section 66 (2) of the Indian Income Tax Act. The reference came before a Bench of this High Court, but in view of a conflict of authorities it was referred by the Bench to the Chief Justice for formation of a Full Bench. As the questions referred to had already been decided by a Full Bench of five Judges this Bench has been formed consisting of seven Judges none of whom have expressed an opinion upon the point.

The assessee is the owner of certain houses in Delhi for which house tax is payable under Section 61 of the Punjab Municipal Act. By a written agreement between the assessee and a tenant, the tenant agreed in addition to the sum reserved as "rent" to pay the amount of tax which under the provisions of the Municipal Act is a tax payable by the owner, that is in this case the assessee. The Income Tax Officer has assessed the property of the landlord under Section 9 of the Income Tax Act. The material portion of Section 9 (1) runs as follows :—

"9. (1) The tax shall be payable by an assessee under the head 'property' in respect of the *bona fide* annual value of property consisting of any buildings or lands appurtenant thereto of which he is the owner." Section 9 (2) is as follows :—

"9. (2) For the purposes of this section, the expression

'annual value' shall be deemed to mean the sum for which the property might reasonably be expected to let from year to year:

Provided that, where the property is in the occupation of the owner for the purposes of his own residence, such sum shall, for the purposes of this section, be deemed not to exceed ten per cent of the total income of the owner."

The Assistant Commissioner for Income Tax included both amounts, that is the amount reserved as rent and the Municipal tax paid by the tenant on behalf of the landlord for the purpose of ascertaining the annual value of the premises. The assessee objected to this procedure on the authority of the Full Bench decision of this Court in *Chunnamal Saligram* v. *Commissioner of Income Tax, Punjab*.

Two questions were referred to this Court. The first question was submitted at the request of the assessee and *Rai Bahadur* Badri Das on his behalf now does-not press this point and withdraws the reference with regard to it.

The second question on which we are invited to express an opinion is as follows:—

"Whether the house tax paid by the tenants of petitioner on account of Delhi Municipal house tax is to be included to arrive at 'the annual value'?'

In our opinion the question to be answered is a simple one. We have merely to construe Section 9 (2) of the Act. "Annual value" in the sub section is clearly defined as "the sum for which the property might reasonably be expected to let from year to year," that is, the sum for which the landlord could let the premises having regard to local conditions and the demand for house in that particular district. The strongest evidence of the sum for which the property might reasonably be expected to let is clearly in our opinion the sum which a tenant would be prepared to pay. It would make no difference what the amount paid to the landlord, or to his use, by the tenant for the right to use the premises was termed. No tenant would in ordinary circumstances pay more than the actual letting value of the premises. If for example there were two houses situated in the same district on the same kind of land and built in the same way, for one the landlord might demand Rs. 110 rent per month; for the other the landlord might demand Rs. 100 rent and insert a condition in

the lease that the tenant should pay Rs. 10 per month, the amount due by the landlord to the Municipality. It appears to us that there can be no distinction between the two cases. In both Rs. 110 a month would be the sum for which the property might reasonably be expected to let.

It is argued in this case that the amount specified to be paid on account of the Municipal tax cannot be included in the sum for which the property might reasonably be expected to let as it was a tax payable by the landlord and that the "annual value" would be the net profit which the landlord actually kept in his own pocket. The basis of the arguments is taken from the judgment of Mr. Justice Tek Chand in the Full Bench case already referred to where he quoted the words used by Mr Justice Wilson in 1885 in *Nundo Lal Bose* v. *Corporation of Calcutta*, that the "annual value of a house" must mean the "annual money benefit derivable from it by the owner." In our opinion, this definition of "annual value" can have no relation to the question before us. "Annual value" in Section 9 of the Income Tax Act is clearly defined. It is not said there that the "annual value" means the "annual money benefit derivable from the property." On the contrary it says that it is the sum for which the property might reasonably be expected to let from year to year. If we may respectfully say so, it appears to us that the decision of the majority of the previous Full Bench of this Court was arrived at by considering other Acts or expressions of judicial opinion which had nothing to do with the construction of this sub-section of the Income Tax Act.

If the argument of counsel is correct that the amount payable to the Municipality on behalf of the landlord by the tenant cannot be included for the purpose of arriving at the annual value there would be nothing to prevent the landlord making an arrangement for the tenant to pay other liabilities of his and so further to reduce the "annual value." There does not appear to us to be any distinction between the tax payable to the Municipality and the land revenue payable in respect of the property. The land revenue is by Section 9 (v) an authorized deduction. It is clear that if the Legislature had meant to authorise any other deduction of the same kind, it would expressly have been included in the allowances."

We have been referred to a case where the same point arose in a reference to the Calcutta High Court and which is reported in *Krishna Lal Seal, In re* which supports our opinion on this question. The reasoning of the learned Chief Justice of the Calcutta High Court in that case appears to us to be un-assailable. The same view was expressed by Addison, J., in the dissenting judgment of our own Full Bench referred to above.

We therefore, answer the reference submitted to us as follows:—

"That in estimating the sum for which the property might reasonably be expected to let from year to year, the amount paid by the tenant of the petitioner on account of the Delhi Municipal house tax should be included, that is, should be treated as part of the rent payable by the tenant to the landlord."

It must, however, be understood that the amount of rent payable by the tenant to the landlord is only *prima facie* evidence or "annual value," and a consideration of the rents paid for similar and similarly situated properties in the locality may show the "annual value" in any particular instance to be less or more than the rent actually paid.

[IN THE CALCUTTA HIGH COURT.]

LAKSHMI NARAYAN SEN & SONS, LTD., *In re.*

SIR HAROLD DERBYSHIRE, C. J., AND COSTELLO, J.

March 10, 1936.

BUSINESS EXPENDITURE—PRIVATE COMPANY—REMUNERATION PAID TO DIRECTORS—WHETHER ALLOWABLE DEDUCTION—POWER OF INCOME TAX AUTHORITIES TO ENQUIRE INTO REASONABLENESS OF REMUNERATION—NATURE OF EXPENDITURE—QUESTION OF FACT—REFERENCE—EXPENDITURE NOT FALLING WITHIN SEC. 10 (2), WHETHER ALLOWABLE—INDIAN INCOME TAX ACT (XI OF 1922), SECS. 10 (2) (ix), 66.

It is nearly always a question of fact whether or not a deduction which an assessee seeks to make under Sec. 10 (2) (ix) of the Indian Income Tax Act, can be properly described as 'an expendi-

ture (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits or gains,' and if the income tax authorities find that it cannot be so described, there can be no reference to the High Court.

Unless an expenditure can be brought under the clauses of Sec. 10, sub-section (2) of the Income Tax Act, it cannot be allowed as a deduction in computing the profits from the business.

Where, in accordance with the articles of association of a private company which authorised the three share-holders of the company who were also its directors to draw an allowance, these directors withdrew Rs. 600 each per month and the income tax authorities, finding after enquiry that a sum of Rs. 175 a month each would be a reasonable remuneration for the services rendered by them, refused to allow the balance of the amount drawn by the directors to be deducted in computing the profits of the company as expenditure solely incurred for earning the profits : Held *(i) that the question whether the payments made to the directors were* bona fide *payments for services rendered or a mere distribution of profits to evade income-tax or super-tax, was a question of fact which the income-tax authorities were competent to go into ; (ii) that the question being one of fact the High Court would not interfere with the finding of the income-tax authorities ; (iii) that the fact that the accounts of the company had been audited and certified by a competent accountant would not preclude the income-tax authorities from enquiring whether such payments were made by way of remuneration for services or as a device to evade income-tax or super-tax.*

Cases referred to :—

ELECTRIC AND DENTAL STORES *v.* COMMISSIONER OF INCOME TAX, BENGAL [1931] (5 I.T.C. 254 ; I.L.R. 12 LAH. 663 ; A.I.R. 1931 LAH. 341 ; 134 I.C. 198).

KESHARDEO CHAMRIA, *In re* [1935] (3 I.T.R. 418 ; I.L.R. 63 Cal. 401).

PAUL AND CO. *v.* COMMISSIONER OF INCOME TAX, BENGAL [1933] (7 I.T.C. 20).

RAMAKRISHNA RAMNATH *v.* COMMISSIONER OF INCOME TAX, C.P. AND BERAR [1929] (4 I.T.C. 171 ; 139 I.C. 290 ; A.I.R. 1932 NAG. 65).

Case stated by the Commissioner of Income Tax, Bengal under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922).

Gunada Charan Sen and *Provas Chandra Majumdar* for the Assessees.

The Advocate-General and *R. C. Pal* for the Income Tax Department.

JUDGMENT.

COSTELLO, J.—The facts of this case are as follows: The assessee is a private limited Company in which three persons Jogendra Sen, Siddeswar Sen and Bankim Chandra Sen (the latter with his two brothers) each holds 100 shares of the nominal value of Rs. 1,000 per share. These three persons hold all the shares of the Company, the business of which consists of money-lending, pawn-broking, the buying and selling of jewellery and is carried on at 62, Chowringhee Road, in this city. The assessment with which we are concerned is for the year 1933-34 and is on the income of the accounting year 1339 B. S. For that year the assessee made a return of income amounting to Rs. 16,222. The assessee was assessed by the Income-tax Officer on a total income of Rs. 37,182. The reason for this was that the Income Tax Officer had found in the course of assessment that in the accounts of the Company a sum of Rs. 7,200 per annum, that is to say, Rs. 600 per month was debited as remuneration paid to each of the three persons whose names I have mentioned and the Income-tax Officer added back that sum to the taxable profits of the Company on the ground that these persons were the sole share-holders of the Company, that the Company maintained a regular establishment including a manager and that the drawings, therefore, represented a distribution of profits and would have been distributed as dividends, had they not been debited and paid out in the guise of remuneration to the same three persons in their capacity as directors of the Company for services which it is alleged they had rendered to the Company.

When the matter came before the Assistant Commissioner on appeal, he directed the Income-tax Officer to enquire what would be the market value of services identical with or similar to those alleged to have been performed by the directors of the Company if such services had been rendered by a stranger and on

receipt of the Income-tax Officer's report the Assistant Commissioner fixed the remuneration of the directors for the services rendered by them at a sum of Rs. 175 a month each, that is to say, Rs. 6,300 in all for the three in the course of the year and the Assistant Commissioner accordingly reduced the income of the Company by the amount. The assessee was dissatisfied with what the Assistant Commissioner had done and accordingly he formulated two questions which he said were questions of law arising out of the decision of the Assistant Commissioner.

The Commissioner of Income-tax did not altogether approve of the form in which the questions were stated and he accordingly redrafted these questions and formulated them as follows :—

(1) "Whether in applying Section 10 (*2*) (*ix*) of the Act, it is within the competence of the Income-tax Officer to go behind the actual payment made and examine if the payment or any portion thereof was or was not on a commercial footing?"
and

(2) "Whether when an expenditure cannot be brought under any of the clauses of Section 10 (2), it can be allowed as a deduction at all in computing the taxable profits or gains of the business?"

These two questions have been referred to us and it is these questions which we are required to answer.

The assessee put forward the contention that the three directors of the Company were authorised to draw an allowance each by virtue of the Articles of Association and he said that each of the Directors had the special qualifications and experience and training necessary for work of the nature required and further that they had a position of great responsibility and therefore the remuneration drawn by each of them was legitimately earned. The assessee put forward the argument that on a proper construction of sec. 10 of the Income-tax Act, the Income-tax Officer could not disallow any payment which had actually been made by a Company to an employee and that in the present instance these directors were in the position of employees of the Company. The assessee then said that though under the provisions of sec. 10 of the Income Tax Act tax must be paid by an assessee on the profits and gains of the business, the Act itself did not specify how these gains were to be computed and therefore they ought

to be computed according to ordinary commercial method, and that after such gains had been computed in this manner sub-section (2) of Section 10 would come into operation with a view to testing whether the principles laid down in cls. (*i*) to (*ix*) of sub-section (2) had or had not been violated. The Commissioner of Income-tax put the matter thus :

" The assessee argues that the allowances paid to the shareholder-directors are admissible deductions and though they may not fall under any specific sub-section of sub-section (2) of section 10, yet they are inherently admissible on a correct construction of Section 10, sub-section (1)".

With regard to the first question the Commissioner came to this finding :—

"The payments made in this case are not *bona fide* payments for services rendered and the payments in question are merely a device for enabling the company to escape super-tax when its profits reach a figure higher than the lowest figure on which company's super tax is chargeable."

The learned Commissioner was of opinion—and, in my view, rightly of opinion—that the matter was really a question of fact ; but he said this :

" as I do not want to deny the assessee any right to which he may possibly be entitled, I think it best to submit the case to the Court."

I am clearly of opinion that this matter was really a question of fact and in this connection I would refer to the case of *Rama Krishna Ramnath Firm of Tirora* v. *The Commissioner of Income-tax, Central Provinces and Berar*. In that case it was held that the

" remuneration paid to a partner doing business in his individual capacity for services rendered to the firm would be a legitimate deduction from the assessable income of the firm ; but sums paid to a partner as such, styled commission, *pagdi* (bonus) or present or by any other name would be simply the profits of the firm appropriated among the owners after they had been earned."

In the case which was then submitted by the Income-tax Commissioner, he said in paragraph 20 of the case :

" The question is really a question of fact. No doubt the

partner in question has a legal personality apart from that of the firm. He might conceivably do business in his individual capacity and in that capacity might render services to the firm in consideration of which the firm might pay him a remuneration which would be a legitimate deduction from the assessable income of the firm. But obviously, considering the opportunities for fraud that any such alleged arrangement would offer, very strict proof would reasonably be required of the existence of such an arrangement, and as a matter of fact, no attempt has been made to prove that such an arrangement exists in the present case."

The view taken by the learned Commissioner was adopted by the Court. At page 178 we find this:

"We cannot interfere with the decision of fact that the assessees have not proved that the arrangement to which the Commissioner refers really existed. The only answer which we can give to questions 5 and 6 is the statement of the law made by the Commissioner of Income-tax."

In the present instance the learned Commissioner refers to the case of *Messrs. B. K. Paul & Co.* v. *The Commissioner of Income-tax, Bengal.* That was a case which came before Sir Charu Ghose (when he was the Acting Chief Justice of this Court), myself and Mr. Justice Ghose. The head-note of the report reads as follows:—

"Where in stating a case referring the question whether remuneration paid as salaries to the adult male members of a Hindu undivided family for services rendered to the family firm, were legally the income of the individual members or an appropriation of the profits of the firm, the Commissioner found, that the alleged salaries were not *bona fide* payments at all to bona fide employees of the business but merely a device to escape income-tax, the High Court returned the reference as not raising any question of law and hence incompetent."

The judgment that was given on that occasion was short and is as follows (at page 25):—

"Having regard to the findings of fact arrived at by the Commissioner of Income-tax and which findings are summarized in paragraph 11 of the letter of reference by the Commissioner, we are not prepared to say that any question of law arises for

our decision in this matter. In our opinion, the Reference, having regard to the said findings of fact, is clearly incompetent. The matter, therefore, will go back to the Commissioner with an expression of our views in manner indicated above."

The principle followed—if there is any principle underlying this case in 7 I.T.C. 20—is very much as that which should govern the present case.

The learned Commissioner seems to have sent the matter to us rather out of sympathy with the assessee and not because he himself was in any doubt as to the answer to the questions which had been formulated. I recall that in a case which came before this Bench in July last—*In re Keshardeo Chamria*—in the course of the judgment which I then gave, I expressed the opinion that where the learned "Commissioner holds that the case rests upon a question of fact, there is no obligation upon him to refer the matter to this Court at all." I think I explained that proposition by adding the words "no necessity whatever." In the present instance, in my opinion, there was no necessity for the learned Commissioner to have referred the present question to this Court, because it nearly always must be a question of fact whether or not the deduction which an assessee seeks to make can properly be described in the words of Section 10 (*2*) (*ix*) as an "expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits or gains." The Assistant Commissioner in the present case, after he had investigated the matter and made enquiries as to what would he the reasonable remuneration for the services of directors in circumstances similar to those in which the directors of the Company with which we are concerned were acting and he having come to the conclusion that Rs. 175 per month would be a proper and reasonable remuneration for the services of the directors and having held that that sum might properly be deducted, that would really be a decision as a matter of fact with which this Court would not be prepared to interfere.

It was argued at the bar that the Income-tax authorities ought not to go behind the accounts—particularly when the accounts had been audited and certified by a competent accountant —for the purpose of ascertaining whether or not the sums which were said to have been paid were reasonable sums by way of

remuneration for the services said to have been rendered. The case I have already cited, *Rama Krishna Ramnath Firm of Tirora* v. *The Commissioner of Income-tax, Central Provinces and Berar* indicates that it is quite competent for the income-tax authorities to ascertain what the real situation is—whether the payments alleged to have been made were in fact made and if they were made whether they were *bona fide* payments made upon a proper basis or whether they really constituted a device for the purpose of evading the payment of income-tax or super-tax. On this point I will refer also to the case of *The Electric and Dental Stores* v. *The Commissioner of Income-tax, Punjab and N.W.F. Provinces.* The head-note is as follows :—

" A decision by the Commissioner of Income-tax allowing partner's salary as a business deduction in the assessment of the firm's pofits in a particular year does not operate as *res judicata* and cannot bind his successor in a subsequent year. Salary charged by working partners in a firm would be admissible as a deduction in the computation of the profits of the firm under Section 10 (2) (ix) of the Income-tax Act, if those partners were true employees and the payment of salary to them was *bona fide* and not a device to escape income-tax."

As I have already indicated, the question whether payments are *bona fide* and not a device must always be a question of fact. It follows, therefore, that we are of opinion that the view taken by the Assistant Commissioner and affirmed by the Commissioner of Income-tax as regards the admissibility of the deduction is the correct view.

It has been conceded in the course of the argument before us that if we agree with the Commissioner of Income tax as regards the answer to the first question, the second question scarcely arises. In any event it seems to me that the answer to that question is obvious and plain. Unless expenditure can be brought under the clauses of Section 10, sub-section (2), it cannot be allowed as a deduction in computing the profits from the business. In my view the matter is correctly stated by the learned Commissioner of Income-tax in the statement of the case. He says with regard to the second question :—

" The assessee contends that all expenses passed by an audi-

tor must be allowed in order to compute the profits or loss of the business for income-tax purposes. In my opinion, this contention is not sound, for while all expenses passed by an auditor are not expenses allowable under the Income-tax Act (e.g., payment of income-tax itself), all expenses allowable under the Income-tax Act are allowable by an auditor. It may be that in computing the 'profits or gains' of a business within the meaning of Section 10 (1) of the Income-tax Act, many items shall have to be deducted though these may not be expenditure at all. Loss occasioned by theft, embezzlement, bad debts, etc., may have to be taken into account for the purpose. The Legislature however is silent on these matters and these may be deductible on the ground that what the section provided for is the assessment of profits and gains of the business and in order to find out such 'profits and gains' we must follow the ordinary commercial method. But so far as allowable items of expenditure are concerned, the Legislature having made express provisions for the purpose of Section 10 (2), I would submit that only those items that are noted there can be allowed."

That statement, in my opinion, is a correct statement of the position.

DERBYSHIRE, C. J.—I agree. The test to be applied is set out in sec. 10 (2) (*ix*) of the Income-tax Act—whether the sums of money allotted to directors are "expenditure" incurred solely for the purpose of earning profits or gains in a business. It has been said that the Articles of Association provide that those sums should be paid by way of remuneration to the directors. That is not conclusive that those sums are "expenditure" incurred solely for the purpose of earning profits or gains in the business. Such a provision in the Articles might be pre-designed to evade the incidence of the proper rate of income-tax. It has been said also that the sums allotted have been passed by the auditors. That again is not conclusive. This is a taxation Act and what is allowable as a deduction is set out in the Act. The taxation authorities, in my view, are entitled to look at the resolutions and look at the provisions of the Articles of Association providing for the directors' salary, but they are not bound by them. They are entitled to consider the fact that the accountant passed the amounts allotted, but they are not bound by that fact. They are

entitled to consider what payments are made for similar services in similar businesses. It is a question of fact in each case as to whether the sums allotted to directors are or are not incurred solely for the purpose of earning profits or gains in a business. In my view no real question of law arises in this matter. The question is whether the Commissioner of Income-tax has or has not properly appreciated and applied the law. In my view he has properly appreciated and has also properly applied the law in this case. The assessee must pay the costs of this Reference.

Reference answered accordingly.

[IN THE PRIVY COUNCIL.]

ASPRO, LIMITED *v.* THE COMMISSIONER OF TAXES.

LORD TOMLIN, LORD THANKERTON, LORD MACMILLAN, LORD WRIGHT AND SIR JOHN WALLIS.

July 27, 1932.

BUSINESS EXPENDITURE—FEES PAID TO DIRECTORS OF PRIVATE COMPANY—RESOLUTION OF COMPANY FIXING FEES—WHETHER CONCLUSIVE—JURISDICTION OF COMMISSIONER TO DISALLOW DEDUCTION.

Two persons were the sole shareholders as well as the sole directors of a private limited company. At the end of each trading year the company fixed at a general meeting about two-thirds of the profits as directors' fees. In the year 1931, a sum of £10,000 was thus debited in the accounts as directors' fees. The Commissioner of income-tax disallowed this item to the extent of £8,000 on the ground that, to that extent, it was not exclusively incurred in the production of the assessable income. The company maintained, in the first place, that the production by them of a resolution fixing the remuneration of the directors for their services and vouchers for payment of the amounts so fixed, when taken with the admitted fact that services had been rendered, was sufficient to exclude any further enquiry by the Commissioner and to entitle them to a deduction, and secondly, that the Commissioner was not entitled to challenge the amount paid by the company to its servants for their services :

Held, (i) *that the first contention of the company was untenable*; (ii) *that, though if the only evidence before the court had been the company's resolution fixing the director's fees and vouchers for payment of the amounts so fixed, it could not reasonably have refused to hold that the assessment was excessive, yet in view of the fact that there was complete identity of the persons interested as shareholders in fixing the amount and of the persons to whom the fees were to be paid and the fact that the fees were fixed each year when a fair estimate of the profits was available, and in view of the other circumstances of the case the court was entitled to hold that the company had failed to prove that the £10,000 had been exclusively incurred in the production of the assessable income.*

Johnson Brothers & Co. v. *Inland Revenue Commissioners* [(1919) 2 K.B. 717; 121 L.T. 645] distinguished.

Appeal from New Zealand.

A. M. Latter, *K. C.*, and *G. O. Slade*, for the appellants.

W. Green, *K. C.*, and *S. R. Blaneo White*, for the respondent.

LORD THANKERTON.—This is an appeal from the judgment of the Court of Appeal of New Zealand dated the 20th August, 1930, dismissing an appeal from a judgment of the Stipendiary Magistrate of the Wellington District, dated the 12th December, 1929, dismissing an appeal against the assessment to income tax made on the present appellants by the present respondent in respect of the year to the 31st March, 1929.

The appellants' trading account for the year to the 31st March, 1928, which fell to be treated as the income year for the purpose of the assessment, showed a debit item of £10,000 in respect of directors' fees, which they claimed as a proper deduction. But the respondent disallowed this item to the extent of £8,000 on the ground that, to that extent, it was not exclusively incurred in the production of the assessable income and he assessed the appellants accordingly; the appellants challenge the assessment in this respect.

The provisions of the Land and Income Tax Act, 1923, as to deductions, so far as material, are as follows:—

" 80.—(2) In calculating the assessable income of any person deriving income from one source only, any expenditure or loss exclusively incurred in the production of the assessable income for any income year may be deducted from the total income

derived for that year...........Save as herein provided no deduction shall be made in respect of any expenditure or loss of any kind for the purpose of calculating the assessable income of any tax-payer.

The Statute provides a special Code by which a tax-payer who is dissatisfied with the assessment made by the Commissioner may appeal against it, but it must first be noted that, under S. 14, the tax-payer is made liable to pay the tax as assessed by the Commissioner " save in so far as he establishes on objection that the assessment is excessive or that he is not chargeable with tax." The special procedure for appeal by way of objections to assessments is contained in Ss. 22 to 38, of which the following provisions are material :—As regards procedure in the Magistrate's Court S. 25 provides—

" On the hearing and determination of all objections to assessments of land-tax or income-tax the burden of proof shall be on the objector, and the Court may receive such evidence as it thinks fit, whether receivable in accordance with law in other proceedings or not."

Where, as here, the amount in dispute exceeds £200, a right of appeal to the Supreme Court from the determination of the Magistrate is given on both law and fact and, on such appeal being taken S. 30 provides that the Magistrate should state and sign a case setting forth the evidence taken before his Court and the questions of law arising for the determination of the Supreme Court. As the present case only raised a question of law, it was removed, with the consent of parties from the Supreme Court into the Court of Appeal under the provisions of S. 33.

It will thus be seen that in the present appeal the power of review of their Lordships is limited to questions of law, and that the appellants have to discharge the burdens laid upon them by Ss. 14 and 25.

The material facts may be summarised as follows :—The company was incorporated in 1923 as a private company, and since then has carried on business in Wellington as manufacturers and vendors of a patent medicine which is known as " Aspro," and sold in tabloid form.

The capital of the company consists of 20,000 fully paid-up shares of £ 1 each, of which Messrs. G. R. Nicholas and A. M.

Nicholas each hold 10,000 shares. These shares, along with £50,000 debentures were given by the company to the Messrs. Nicholas as consideration for an exclusive licence to use the trade mark "Aspro" and to deal in the commodity in New Zealand. Throughout the existence of the company, the Messrs. Nicholas have been the sole directors of the company as well as the sole shareholders.

The company's trading year ended on the 31st March in each year, the first year's accounts covering only nine months' trading. The directors' fees were fixed towards, or after, the end of each trading year. The following table shows the amount of the fees in each year, the date when they were fixed and the net profits left to the company after deduction of the fees—

Year ending.	Date directors' fees were fixed.	Fee fixed for each Director.	Net profit left to Appellant.
31st March 1924.	27th March 1924.	£ 1,500	£ 1,418 9 10
31st March 1925.	16th March 1925.	,, 2,500	,, 2,616 14 10
31st March 1926.	1st July 1926.	,, 3,250	,, 3,170 11 8
31st March 1927.	21st June 1927.	,, 5,000	,, 4,924 13 7
31st March 1928.	8th June 1928.	,, 5,000	,, 5,145 6 6

These fees were fixed each year by resolution of the company in general meeting. The company having adopted Table "A" of the New Zealand Companies Act, 1908, the remuneration of the directors is provided by Art. 78, which is as follows :—The directors shall be paid out of the funds of the company, by way of remuneration for their services, such sum or sums as the company may from time to time fix at a general meeting, and such remuneration shall be divided amongst them in such proportions, as the directors may determine." Prior to the year ended in March 1928, their amount so fixed was accepted as a proper deduction for income tax purposes by the Commissioner.

The two directors in question reside in Melbourne and direct the policy of the New Zealand Company from there. The parent company is an Australian Company and there is also a subsidiary English Company, and the Messrs. Nicholas are also directors of those two companies. A comparison of the monthly sales of these three companies shows that the volume of the Australian business is about eight times and the volume of the English

business about eleven times, that of the New Zealand business. There is a local manager in Wellington, who acts under the direction of Melbourne: weekly samples of the mixture made in Wellington are sent to Melbourne which are tested by Mr. G. Nicholas and the result is reported by him to Wellington. The manager stated that about three letters each way would pass between Wellington and Melbourne, and that about one letter in six of those sent by him would be referred to the directors. While it was stated that the directors paid periodical visits to New Zealand it was admitted that neither of them had been in New Zealand in the year in question. They declined to give the respondent information as to the amount of time spent by them in New Zealand since the inception of the company, and neither of them appeared to give evidence before the Magistrate.

The appellants maintained in the first place, that the production by them of a resolution fixing the remuneration of the directors for their services in terms of Art. 78, and vouchers for payment of the amounts so fixed, when taken along with the admitted fact that service had been rendered, was sufficient to exclude any further enquiry by the Commissioner and to entitle them to a deduction in terms of Section 80 (2) of the Act. But this contention was not seriously pressed, and in their Lordships' opinion, it is untenable.

The appellants maintained, in the second place, that the Commissioner was not entitled to challenge the amount paid by the company to its servants for their services on the ground of excess or over-generosity in its amount, for that was entirely a matter in the discretion of the company, and that he could only challenge such payments on the ground that it was not a genuine transaction, being in fact fictitious or the sums so paid being, wholly or partly, not truly paid as remuneration for their services. They maintained that in the present case, there was no evidence to justify any such ground of challenge by the Commissioner and that, accordingly, the Magistrate was bound to sustain the appellant's objections and to hold that the assessment was excessive. The respondent substantially accepted the premises of this contention, but he maintained that the state of the evidence was such that the appellants had failed to establish that

the assessment was excessive, as required by Section 14 or to discharge the burden of proof laid on them by Section 25.

In their Lordships' opinion, there is no material difference betwen these two aspects of the argument for present purposes, and the true issue is whether there wes evidence before the Magistrate on which he was entitled to refuse to hold it proved that the £ 10,000 had been exclusively incurred in the production of the assessable income and that the assessment was excessive. If the only evidence before him had been the company's resolution fixing the directors' fees and vouchers for payment of the amounts so fixed, it is difficult to see how the Magistrate could reasonably have refused to hold that the assessment was excessive and the question must be whether there was further evidence which reasonably entitled the Magistrate to decline to hold it proved that the assessment was excessive.

Their Lordships are of opinion that the state of the evidence was not such as to compel the Magistrate to the conclusion that the £ 10,000 had been exclusively incurred in the production of the assessable income. There was complete identity of the persons interested as shareholders in fixing the amount of the fees to be paid to the directors and of the persons to whom the fees were to be paid, and, except in regard to its bearing on the liability of the company to tax, it made no difference to the destination of the money whether the amount of the fees represented fair remuneration for the directors' services or not. The Messrs. Nicholas, who, as sole shareholders and sole directors alone knew how the fees came to be fixed, not only declined to allow the respondent to examine them on this matter, but did not come forward to give evidence before the Magistrate, although the burden of proof was upon them. Further, in this situation, it is not irrelevent to take also into account that in each year the fixing of these fees was made when a fair estimate of the trading results for the year was available and that in each year, of the balance available for directors' fees and for distribution among the shareholders, about two thirds was apportioned to directors' fees. In their Lordships' opinion, the Magistrate was entitled to hold that the appellants had failed to prove that the £ 10,000 had been exclusively incurred in the production of the assessable income.

None of the authorities cited appear to have much bearing on the present case, except possibly the case of *Johnson Brothers and Co.* v. *Inland Revenue Commissioners* in which the sums paid to the owner's sons, who were employed in the business were disintegrated, on the evidence of the owner himself, into the amount of a fair wage and a balance which might be considered as paid on account of family feeling"; but there was nothing equivalent to the resolution of the company in the present case.

For these reasons their Lordships are of opinion that the judgments appealed from were right and that the appeal should be dismissed with costs, and they will humbly advise His Majesty accordingly.

Appeal dismissed.

Solicitors:—*Stafford, Clark & Co.*, for the appellants; *Mackrell, Maton, Godlee and Guincey*, for the respondent.

[IN THE PRIVY COUNCIL.]

COMMISSIONER OF INCOME TAX, BENGAL

v.

THE HUNGERFORD INVESTMENT TRUST LTD.

LORD ROCHE, SIR SHADI LAL AND SIR GEORGE RANKIN.

May 26, 1936.

COMPANY—DIVIDENDS—EXEMPTION FROM INCOME TAX—DIVIDEND REPRESENTING FOREIGN INCOME NOT ASSESSABLE IN INDIA—WHETHER EXEMPT FROM INDIAN INCOME TAX—INDIAN INCOME TAX ACT (XI OF 1922), SEC. 14 (2) (a).

Under Section 14 (2) (a) of the Indian Income Tax Act where the profits and gains of a company have been assessed to income tax any sum which a person receives by way of dividends as a shareholder is exempt from income tax. The fact that the company's profits and gains included specified sums which were not assessable and were not assessed, to income tax under Section 4 of the Indian Income Tax Act, will not render such proportion of the dividends as

the specified sums bear to the aggregate of the total profits, liable to income-tax.

The Hungerford Investment Trust Ltd., a company registered outside British India held the whole of the ordinary share capital in Turner Morrison and Co., a company registered in British India. The profits and gains of the latter company for the years 1930 and 1931 included a sum of Rs. 76,500 which was distributable as dividend but was not assessable to Indian income-tax as it did not accrue or arise within British India. Dividends were declared in the year 1931. The question being whether such proportion of the divinends paid to the Hungerford Investment Trust Ltd., as the sum of Rs. 76,500 bore to the aggregate profits of 1930 and 1931 was also exempt from income tax under Sec. 14 (2) (a) of the Indian Income Tax Act: Held, *affirming the decision of the Calcutta High Court, that the phrase 'where the profits and gains of the company have been assessed to income tax' in Sec. 14 (2) (a) must the construed in its natural meaning and the entire dividend paid to the Hungerford Investment Trust Ltd., was exempt from income-tax under Sec. 14 (2) (a), even though the sum of Rs. 76,500 had not been assessed to income-tax in the hands of Turner Morrison and Co.*

A. M. Dunne and *T. N. Donovan,* for the Appellant.

Gavin T. Simonds, F. Grant and *A. G. Pullen,* for the Respondents.

JUDGMENT.

SIR GEORGE RANKIN.—This appeal is brought by the Commissioner of Income Tax, Bengal, from the decision of the High Court at Calcutta upon a reference made under S. 66 (2), of the Income tax Act (XI of 1922). Two questions were originally referred to the High Court for its opinion, but the assessee made an admission which rendered the first question unnecessary. The sole question before the Court was as follows:

The assessee's income in assessment having included dividends declared on 16th April 1931, and 3rd November 1931 by a company whose profits of 1930 and 1931 were found to include specified sums to which in accordance with S. 4 the Act did not apply; and the said company having been assessed in respect of profits to which the Act did apply, in such proportion of the dividends, as the specified sums bear to the aggregate of all profits in

1930 and 1931 respectively exempted from taxation to ordinary income-tax in accordance with Section 14 (2)?'

The question arises out of the assessment for the year 1932-33 to be made upon the Hungerford Investment Trust, Ltd., a company registered outside British India which will be herein referred to as "the assessee." The assessee holds the whole of the ordinary share capital in a company called Turner Morrison & Co., Ltd., registered in India, which will be herein referred to as "the company." In the year of the account 1931-32 the assessee received as dividend upon its shares in the company, two sums as follows, namely, (a) rupees three lakhs being final dividend declared on 16th April 1931, by the company in respect of the calendar year 1930, and (b) rupees one and a half lakhs being an interim dividend declared on 3rd November 1931, by the company in respect of the calendar year 1931.

The profits and gains of the company for the year 1930 were assessed to Indian income-tax in the year of assessment 1931-32. On the basis of that investigation the Commissioner for Income-tax purports to find as facts that 2 per cent of the company's profits and gains in 1930 consisted of interest on tax-free securities of the Government of India; that 12 per cent consisted of profits or gains which did not accrue or arise within British India, and which were not received in British India, or deemed so to be, and which accordingly were not profits or gains to which the Act applies; and that the remaining 85 per cent of the company's profits in 1930 were subjected to Indian income-tax in the hands of the company in the year of assessment 1931-32. By a similar investigation into the profits and gains of the company for 1931 it was found that 1 per cent of the profits made by the company in that year consisted of interest upon tax-free securities of the Government of India, 25 per cent consisted of sums to which the Indian Income-tax Act did not apply and the remaining 74 per cent was chargeable to income-tax under the Act.

Applying these proportions to the two sums received by the assessee by way of dividend from the company in the year of account 1931-32, the Commissioner has disintegrated the total sum of Rs. 4,50,000 into three parts treating Rs. 7,500 as referable to interest on tax-free securities of the Government of India within the meaning of Proviso 2 to Sec. 8 of the Act; Rs. 76,500

as dividend derived from distributable profits of the company not taxable in the hands of the company within S. 4 (1) of the Act, and Rs. 3,66,000 as dividend derived from profits and gains of the company chargeable with income-tax. The question before the Court has reference only to the second of these three sums, namely Rs. 76,500, and that question has in the end to be answered by arriving at the true construction of Cl. 2 (a), S. 14 of the Act which is in the following terms:

'14.—(1) The tax shall not be payable by an assessee in respect of any sum which he receives as a member of a Hindu undivided family.

(2) The tax shall not be payable by an assessee in respect of:

(a) any sum which he receives by way of dividends as a shareholder in a company where the profits or gains of the company have been assessed to income-tax; or

(b) such an amount of the profits or gains of any firm which have been assessed to income-tax as is proportionate to his share in the firm at the time of such assessment; or

(c) any sum which he receives as his share of the profits or gains of an association of individuals, other than a Hindu undivided family, company or firm, where such profits or gains have been assessed to income-tax.'

The Indian Income-tax Act, as Ss. 19 (a) and 23 make clear, requires a return to be made by every company, as well as by every person other than a company whose total income is, in the Income-tax Officer's opinion, of such an amount as to render such person liable to income-tax. This brings about the principle or method which is sometimes described as double assessment and sometimes, as assessment at the source (as distinct from deduction at the source which is employed in the case of "interest on securities" and "salaries". The method of double assessment is applied not only in the case of companies but in the case of firms, Hindu undivided families, and other associations of individuals. When a company has made its return of the profits and gains in the year of account, that is, of what the Act calls the "total income" of the company during the previous year, the Income-tax Officer, if satisfied that it is correct and complete, is directed by S. 23 (1) that he shall assess the total income of the assessee and shall determine the

sum payable on the basis of such return. If the return is not correct or complete the same result is to be arrived at after taking further proceedings as described in the section. The like process is carried out in respect of the return made by the individual shareholder if he is chargeable with Indian income-tax at all.

As part of his total income, he has to include the dividend which he has received from the company during the previous year in order that his " total income " within the meaning of the Act may be ascertained, a figure which is necessary if only to fix the rate of tax payable by him in the year of assessment. Sec. 14 contains directions to the effect that certain sums which have been received by the assessee in the year of account and which are part of his " total income " within the meaning of the Act are to be free so far as payment of the individual is concerned, the reason being that although companies, firms and other associations are as such subjected to assessment, double assessment is not intended in all cases to carry with it the consequence of double payment. If, for example, the Hindu undivided family has been assessed in respect of a sum, the part which the individual member has received is not to be taxed for the second time in his hands. If a firm of three partners have been assessed to tax upon their profits the partner is not to pay again upon his share of the same profits. Cl. (a) of sub-s. 2 is a more or less similar provision in the case of a company paying dividends. Its object is to ensure that tax shall not be paid more than once upon what the statute regards as the same thing. The company though a separate legal persona in the contemplation of law and liable to assessment as a subject chargeable with tax is not for all purposes to be regarded as entirely separate and distinct from the corporators. The underlying principle of the clause as the Commissioner in stating the present case has recognised is " that the dividend represents merely the shareholders' share in the income of the company."

To arrive at a true construction of S. 14 (2) (a) it is necessary to consider all references in the Act to " profits and gains "—in particular S. 4 and the definition of total income in S. 2 (15) of the Act: also Ss. 20 and 48. Certain arguments have been drawn from the language of Cls. (b) and (c) of sub-sec. 2 of S. 14, but it is difficult to regard them as decisive in favour of

either side to the controversy. The contention on the part of the assessee is in effect that Cl. 14 (2) (a) is satisfied in any case in which the company has been assessed to income-tax in respect of its profits or gains in the relevant year. If it has been assessed at all it has presumably been assessed upon its "total income" within the meaning of the Act; and the fact that it may have been in receipt of sums distributable to Indian income-tax because not profits or gains to which the Act applies, does not, upon this view, prevent the clause from freeing the dividend received by the shareholder from any further payment of tax.

The view contended for by the income-tax authorities has been put in different ways. The Commissioner of Income-tax in giving his opinion upon the reference, drew a distinction between income, that is specially exempt under the Act, *e.g.*, agricultural income, or income from tax-free securities, and what he calls (somewhat unfortunately having regard in particular to Section 34 of the Act) "income that has merely escaped assessment," by which he means profits and gains that are not chargeable to Indian income-tax because they have neither accrued nor been received in India. With regard to the former he admits the applicability of the principle before mentioned that a dividend represents merely a shareholder's share in the income of the company. With regard to the latter he rejects this principle as "it cannot be said that the place of receipt by the company constitutes a characteristic of the income which is retained, against the actual place of receipt by the shareholder, when the income passes on to the shareholder." In his view, Section 14 is among "provisions for the avoidance of levying the tax twice over upon the same accrual—it is important to avoid calling it the same "income." These observations of the Commissioner were doubtless made with specific reference to the first of the two questions originally stated, a question with which their Lordships are not now concerned, but it is important to notice that it is impossible to suggest any construction of Cl. (a) of Section 14 (2) which would make the clause discriminate between these two classes of income which are not charged with tax. Whether it be that the legislature has not sufficiently appreciated the importance of the distinction between the same accrual and the same income, or has given unexpected weight to the principle that a dividend represents merely

the shareholders' share in the income of the company, the distinction drawn by the Commissioner cannot in their Lordships' view be discovered in the clause.

Before the High Court of Calcutta the contention put forward by the Advocate-General was that the clause only applied where the whole of the profits of the company had been assessed to income-tax, that is to say, where the "total income" within the meaning of the Act contained everything that was distributable as profit. If this view be accepted it is true, as Panckridge, J. observed, that some startling results would follow. In the first place, every shareholder in a bank, insurance company or other company whose profits and gains consist in part of interest from tax-free securities would be taxed again upon the whole of his dividend, and the same would apply in the case of a company with agricultural income. This is an impossible conclusion, as sufficiently illustrated by the circumstance that the Commissioner in the present case does not claim to charge the assessee with tax upon the sum of Rs. 7,500, being the proportion of the assessee's dividend which he brings within the ambit of the second proviso of Section 8. Indeed it is clearly inadmissible to read "all the profits or gains of the company have been assessed" or "the total profits or gains" in expansion of the phrase used by the section, since even if it could he shown that some of the assessable profit of the company had escaped assessment it cannot be supposed that instead of dealing with the matter under Section 34 by making an additional assessment on the company the Income-tax Officer is to be at liberty to raise it *vis a vis* the individual shareholder. Before the Board, however, another construction of clause (a) was propounded. It was stated in the appellant's case as reason No. 5:

'Alternatively because Section 14 (2) confers exemption only upon that part of the aforesaid dividends, which was paid, or may be taken to have been paid out of the profits of Turner Morrison & Co., which were assessed to income-tax.'

The view may perhaps be put by saying that Cl. 14 (2) (a) should be read to mean that the tax shall not be payable by an assessee in respect of any of the profits or gains of a company which the shareholder receives by way of dividend where such profits or gains have been assessed to income-tax, or again, that

tax shall not be payable by an assessee in respect of any sum which he receives by way of dividends . . . to the extent to which the profits or gains of the company have been assessed to income-tax. This, which may be called a distributive construction of Cl. (a), cannot be dismissed on the ground that the meaning given to the clause is unreasonable in itself. It is, however, very difficult to think that it is the true meaning of the clause. One would not expect the phrase "where the profits or gains of the company have been assessed" to be used in such sense as to point to the possible existence of receipts which are not profits or gains within the meaning of the Act at all, or at least are not part of the company's "total income" but profits or gains to which the Act does not apply. It is not readily to be assumed that the Act intends the Indian Income-tax authorities to investigate and settle the exact amount of such "profits and gains"—involving as this process must, receipts which have never accrued or been received in India or brought to India, and expenditure made in the course of carrying on business in another country. The terms of S. 20 providing for a certificate to be given by the company do not assist such a construction of S. 14 (2) (a). Again, the vagueness of this construction makes it somewhat incredible.

It may be that on any view the clause does not make clear whether the contemplated assessment of the company's profits has reference to the same year of assessment as the shareholder is concerned with, and, if not, how the relevant year is otherwise to be ascertained. But if the sums available for distribution by a company under the company law are to be examined and disintegrated, one would not merely desire but expect directions on the question whether, in the case of dividends paid out of accumulated profits, the dividends received by the shareholder were to be free of further payment if the company had paid tax on the relevant profits at any time and at any rate prevailing at the time. A construction which raises so important a matter and then leaves it utterly at large is not without great difficulty. It is also to be observed that the construction proposed assumes that it is possible and reasonable to ascertain whether and to what extent a particular dividend represents, to use a neutral term, profits brought to charge in the hands of the company. No doubt a rule

of proportion can be applied as is proposed in the present case, but no such rule has been laid down by the Act and the construction contended for involves difficulty in the absence of a rule. Indeed the Commissioner himself has not unreasonably argued that in the case of dividends it is not possible to say what funds they were paid from: "Payments are made out of one pool of liquid assets on account of one liability or another. There is no separate pool of profits—still less of each separate type of profits." He suggests, however, that the legislature intended to leave "this very difficult relation of the dividends and the profits to be wholly determined as facts."

In the case before the Board, in order to obtain an authoritative ruling on the construction of Cl. 14 (2) (a), an admission has been made by the assessee that no part of the sum of Rs. 76,500, now in question, was paid out of profits which had at any time been assessed to Indian income-tax. Still, in construing Cl. (a), their Lordships have to consider whether the proposed construction which ignores this difficulty can be accepted. What is involved in leaving the relation between the dividends and the profits to be determined as facts can be seen from annexure (d) (2) to the letter of reference where the Assistant Commissioner in dealing with the assessment of Turner Morrison & Co., Ltd., (to which in the present case he referred for his reasons) stated:

'The assessees further contend that the Companies did not bring the foreign income to India but declared the dividend out of the Indian income but I don't think it is possible to split up the income in such a manner in declaring the dividends. The dividends are declared out of the total income of the company.'

If the construction contended for involves that the income-tax authorities are to find something as matter of fact which is not matter of fact, that again is an infirmity of some importance and it is not made better by the circumstance that there is small chance of evidence to fetter them in their findings. No doubt the case may be put of a company in which only the smallest fraction of its distributable profit has been received in India and become chargeable to Indian income-tax, and where, notwithstanding this fact, by some process of borrowing or otherwise the rest of the real profit or part thereof is being distributed among share-holders in India. It is however, difficult to be sure that

the legislature was so dissatisfied with the provisions of Section 4 (2), (as they stood before 1933) as to assume that it rendered probable any important leakage by this means. It has been suggested that the wording of Section 48 (1) assists the contention of the income tax authorities but that section throws little light upon the meaning of Cl. (a) of Section 14 (2).

Their Lordships have to be satisfied as to the meaning of Cl. (a). In their opinion it was rightly construed by the High Court of Calcutta who have given to the phrase "where the profits and gains of the company have been assessed to income-tax" its ordinary and natural meaning. This in itself is a sufficient ground of decision, but their Lordships are satisfied that any departure from the immediate and direct meaning of the phrase leads to difficulties of interpretation and to results which cannot be imputed to the legislature as within its intention. The answer to the question propounded is in the affirmative. Their Lordships will humbly advise His Majesty that this appeal should be dismissed with costs.

Appeal dismissed.

Solicitors for the Appellant—*The Solicitor, India Office.*

Solicitors for the Respondents—*Sanderson Lee & Co.*

[In the Patna High Court.]

LACHIRAM BALDEODAS

v.

COMMISSIONER OF INCOME-TAX, BIHAR AND ORISSA.

Wort, acting C. J., and Dhavle, J.

May 7, 1936.

Hindu Undivided Family—Application for Registration as Firm—Absence of Evidence to Prove that Family Property was Divided—Duty of Income Tax Officer—Scope of Inquiry—Burden of Proof of Partition—Indian Income Tax Act (XI of 1922), Secs. 25-A, 26-A.

Under Section 25-A of the Indian Income Tax Act the Income Tax Officer does not inquire into a question of separation or dis-

ruption of the family, notional or otherwise; he has to inquire into the question of whether the joint family property has in fact been divided, and where there is no evidence to show that the family property has in fact been divided and it is not suggested that a partnership exists alongside the joint family firm, an income-tax officer would be justified in coming to the conclusion that the partnership alleged to exist between the members of the family is not genuine and in declining to register members of the family as a firm under Sec. 26-A.

The question whether a family is joint or separate is substantially a question of fact.

Where an application is made under Sec. 26-A, it is for the applicant to establish the fact that a partnership had come into existence and that that partnership was to be assessed in substitution for the Hindu joint family which had been dssessed heretofore as such.

BISSESWARLAL BRIJLAL *v.* COMMISSIONER OF INCOME TAX, BENGAL [1930] (I. L. R. 57 Cal. 1336; 34 C. W. N. 363; 128 I. C. 327; A.I.R. 1930 Cal. 449; 4 I.T.C. 365) *referred to.*

Case stated by the Commissioner of Income-Tax, Bihar and Orissa under Sec. 66 (3) of the Indian Income-Tax Act [Misc. Judicial Case No. 3 of 1935].

K. P. Jayaswal and *J. C. Sinha*—for the assessee.

Manohar Lal—for the Commissioners.

JUDGMENT.

WORT, AG. C. J.—This is a case stated by the Commissioner of Income-tax under the direction of the Court and the question submitted for consideration was "Under the circumstances of this case is the family to be considered joint or separated in law?" There is no doubt that that question, that is to say, whether the family can be considered joint or separate, is substantially a question of fact: but it is contended shorty by Mr. Jayaswal on behalf of the assessee that in the circumstances of the case there was no evidence upon which the Income-tax Officer, and ultimately the Assistant Commissioner and the Commissioner could decide against the application which was made by the

assessee to be registered as a firm under S. 26-A, Income-tax Act. The case has been very elaborately argued; but in my judgment the matter is resolved by a very simple consideration. Shortly stated, the family of Lachhiram had been assessed as a joint Hindu family up to 1931; the year of assessment in dispute is the year 1931-1932. Lachhiram's family was carrying on business as a joint Hindu family and in 1931 three members of that firm being the sons of Lachhiram, Baldeodas, Mulchand and Mahabir Prasad, executed what purported to be a deed of partnership. This was on 1st June of that year and in the month of August following they made an application to the Income-tax Officer under S. 26-A, Income-tax Act, to be registered as a firm. In the result that Income-tax Officer decided that the alleged partnership was fictitious, not being acted upon, and that the members of the family still remained a joint Hindu family.

Now Mr. Jayaswal contends in substance that the apparent state of facts should be taken as real in the absence of any evidence to the contrary and he contends that the inquiries which were made by the Income-tax Officer and upon which he appears to have decided that the family was still joint were not evidence upon which he was entitled to come to the conclusion that this partnership deed was an unreal transaction. The Income-tax Officer relied upon inquiries made from outsiders; he also found that the parties were messing together, and also a matter which in his opinion was of considerable importance was the fact that the father Lachhiram did not execute the partnership deed to which I have already made reference. I should be more accurate in saying that the Income-tax Officer stated that the father did not endorse the partnership deed. His statement to that effect was made for obvious reasons. It is nowhere contended that Lachhiram was a partner in the new firm and therefore it would be unnecessary to execute it; but the Income-tax Officer in making a reference to this fact stated that it was recited in the partnership deed that the members of the family had separated and it is in reference to this statement that the Income-tax Officer was of the opinion that the endorsement of Lachhiram might have been or was necessary and its absence raised a suspicion, which added to the facts of the case and made him come to the conclusion to which I have already referred.

As I have already stated, whether the partnership transaction was real or not is purely a question of fact. The matter seems to me to be concluded by what I have already described as one which was of considerable importance for consideration. Mr. Jayaswal would have this Court to hold that the effect of the Income-tax Officer's finding is a finding of fact against the assessee, and in order to come to that conclusion definite evidence is required which in this case it is contended is absent.

Now the points which seem to me to determine this question are very simple. The applicant applied under S. 26-A, as I have already stated, and it was for him to establish the fact that a partnership had come into existence and that partnership firm in the future was to be assessed in substitution for the Hindu joint family which heretofore had been assessed as such. Shortly stated, the Income-tax Officer was not satisfied with that transaction and when the matter comes to be examined it seems to me that transaction is something more than a matter of suspicion. The mere application under S. 26-A and a decision even in favour of the assessee would not conclude the matter, and for this reason: Lachhiram had three sons, two of whom I have mentioned, the third was Hazarimul who is now represented in the partnership transaction by his son Mahabir Singh who was his adopted son. There was Debi Prasad who was the son of the second member of the alleged partnership, that is to say, the son of Mulchand, and there were at least four sons of Baldeodas. It will be seen that as Lachhiram and the sons of whom I have made mention were not partners under the partnership deed, in one form or another either the joint family or several joint families remained and the mere decision of the Income-tax Officer under S. 26-A that three persons had constituted themselves a partnership firm, would not settle the question of whether there was to be in future an assessment on the joint family or more than one joint family. It is important to notice this in connexion with a matter to which I am now about to refer. Mr. Jayaswal contends that it was unnecessary for him to make an application under S. 25-A, Income-tax Act. That section provides:

Where at the time of making an assessment it appears that there has been a separation between the members of the family

who have been assessed as such, and that the joint family property has been partitioned among the various members or groups of members in definite proportions, he shall record (that is to say the Income-tax Officer shall record) an order to that effect.

It was never the case of the assessee either before the Income-tax Officer or the Commissioner or before this Court, although it was faintly suggested by Mr. Jayaswal, before this Court, that the partnership firm existed alongside the joint Hindu family, and as it was nowhere stated, as I have already stated in order to finally decide the question of assessment, it would have been necessary for an application to have been made and a decision to have been given under S. 25-A for the reasons which I have already indicated. In those circumstances as no application was made, and in order to test whether in future this partnership firm should be substituted for the joint Hindu family that has been heretofore assessed, it was not only possible, but it was the only course which the Income-tax Officer could take in the circumstances, to inquire whether in fact the joint Hindu family property had been divided. Under S. 25-A the Income-tax Officer does not inquire into a question of separation or disruption of the family, notional or otherwise; he has to inquire into the question of whether the joint family property has in fact been divided, and having regard to the fact to which I have already referred, that it is not suggested that the joint Hindu family firm existed alongside the new partnership firm, it is not surprising that the Income-tax Officer, in this case, in the absence of evidence that the property of the family had been divided, came to the conclusion that the partnership transaction was not a genuine one.

Now Mr. Jayaswal contends on the other hand that there are two items of evidence which do in fact prove that the joint family property was divided and that neither the joint family nor the joint family property hereafter existed. The evidence to which reference was made was first a deed of relinquishment entered into by Baldeo Das, Mulchand and Mahabir Prasad and various minor members of the family and Lachhiram, the father, that purported to relinquish the rights of the parties in the property in favour of their father Lachhiram. It is difficult to know exactly what effect in law this deed would have if the family were joint. It is perfectly obvious that they could not execute

such a document, at any rate a document such as this could not take effect. In any event the deed of relinquishment is not a document of title, and thirdly it is to be noticed that the mention of the properties and the relinquishment of the rights of the parties in them in favour of the father indicate, taken in conjunction with the evidence of Baldeo Das taken on oath before the Income-tax Officer, that there were properties other than those mentioned in the deed. But apart from that, the deed does not purport to be a partition deed; it may relinquish some properties in favour of the father, but, as I have already indicated, there are properties which are not the subject matter of this deed and in those circumstances in my judgment it is impossible to say that that evidence by itself was such that the Income-tax Officer was not entitled to come to any other conclusion than that the property had been divided as alleged.

The other piece of evidence is the account in the *bahi* dated 28th June 1930 in which the accumulated profits are shown to be divided between the three members of the firm and the father Lachhiram. In this account Lachhiram gets a share of approximately Rs. 24,000 less than the others which it is stated is made up by moveable property which had been released under the deed of relinquishment. It was some evidence possibly that the joint family property had been divided, although it is stated by the Income-tax Officer to be a division of the accumulated profits; but it is, in my judgment, impossible to say that it was such evidence that the Income-tax Officer was bound to come to the conclusion that the fact had been proved that the joint family property had been divided. Reference has been made by Mr. Jayaswal to declarations made on different dates as to the separation of the family in contradistinction to the division of the property. One was made in 1933 before the Agent of the Imperial Bank, but the fact that it was so late as 1933 is in itself significant. The partnership deed was entered into in June 1931; there was a gap therefore of a year or two before the declaration was made before the Imperial Bank. The weight of this evidence is not a matter for this Court.

The fact that the declaration was made is stated in the report made by the Income tax Officer, but if any criticism were necessary it is to be found in the fact that the declaration was made

in 1933 whereas the partnership was entered into in June 1931. We can assume (and we must assume) that Baldeo Das who acted as the manager of the firm had up to that time operated on the account; and the necessary question which arises is what was happening between June 1931 and 1933 when the declaration was made? It rather indicates that at any rate during that period, although that partnership deed was in existence, the members of the partnership did not treat themselves as such. As I have already stated this is not a matter for this Court but was one of the questions which influenced the mind of the Income-tax Officer and it is impossible therefore to hold that he was not entitled to be so influenced. Shortly stated, the matter comes to this: in the circumstances of the case the Income-tax Officer had to be satisfied that the joint family property had been divided. I say that by reason of the facts of the case which had been put forward by the assessee before him under the application under Section 26-A. That being so, although there was some evidence it was not evidence on which he was obliged to act and he came to the conclusion that the property had not been so divided. That being so the only conclusion which he could have arrived at on the application made under S. 26-A was that the partnership transaction was not a real one. The case is not unlike that reported in *Bisseswarlal Brijlal* v. *Commissioner of Income-tax*, in which a partnership deed alone had been adduced in evidence before the Income-tax Officer. Sir George Rankin pointed out that that was the only evidence before the Income-tax Officer upon which he was asked to act. It was for the applicant to establish the fact that the partnership existed and it was, to use the words of Sir George Rankin:

"Tolerably clear in the absence of some evidence to the contrary, that this piece of paper referring to the partnership deed which the parties had signed was expected to be magical talisman which would protect them from the imposition of super tax and had no other reality at all."

It is contended as I have already stated that there was evidence in this case. It is true that there was evidence, but the weight of that evidence was for the Income-tax Officer as also the conclusion at which he should arrive. It is impossible to hold that in this case the Income-Officer was not entitled to

come to the conclusion which he did. That in my judgment is sufficient and the answer to the case submitted by the Commissioner of Income-tax, is that in the circumstances of this case the family is to be considered joint. The application is dismissed with costs : hearing fee Rupees two hundred and fifty.

DHAVLE, J.—I agree. When the assessee first came up to this Court his grievance substantially was that the refusal of the Income-tax authorities to register the firm was wrong and arbitrary; and he got this Court to direct the Commissioner to state a case on the point whether in the circumstances of this case the family was to be considered joint or separate in law. Partnerships are dealt with in S. 26-A of the Act, and the question which the Income-tax Commissioner was required to state is a question that is dealt with in S. 25-A of the Act. As regards the question under 26-A, no appeal lay at the time the assessee's application was disposed of by the Income-tax Officer, but there was an appeal provided by law at the time against orders under S. 25-A. It was obvious how in the circumstances of this case the two questions were connected together. Some of the argument before us has proceeded on the footing of what is called the notional separation of a Hindu joint family which sometimes gave rise to very difficult questions of law ; and the legislature has got over the difficulty by enacting specially in Section 25-A of the Act that what the Income-tax authorities have to proceed upon is whether " the joint family property has been partitioned amongst the various members or groups of members in definite proportions. That is a concrete question of fact which it is fairly easy to investigate.

It has been contended on behalf of the assessee that in view of the deed of partnership and the *ladavi* deed and the accounts put forward on behalf of the assessee it was not open to the Income-tax authorities without any material whatsoever to treat these documents as bogus, but it is not a fact that the Income-tax authorities have proceeded without any material at all. They were entitled to take the circumstances into account, particularly the delay in the declarations of separation made by the members of the family to the Imperial Bank and elsewhere, and the statement I find made in the tenth ground of the assessee's application to this Court that the petitioners never thought it necessary to

make it known to the outside world that there had been a disruption in the family when their close friends and relatives knew about it. Whether in the circumstances of this case there had been what the Income-tax Commissioner calls an actual separation of the family, or as S. 25-A of the Act puts it, a partition of the joint family properties amongst the various members or groups of members in definite proportions, was clearly a question of fact. I do not think that on the materials produced before the Income-tax authorities by the assessee there could in law have been a decision one way only and this, as my Lord the Chief Justice has observed, is sufficient to dispose of the reference.

Reference answered.

[IN THE LAHORE HIGH COURT.]

NAWAL KISHORE KHARAITI LAL

v.

COMMISSIONER OF INCOME TAX, PUNJAB & N. W. F. P.

SIR JAMES ADDISON AND ABDUL RASHID, JJ.

March 16, 1936.

INCOME TAX—ENHANCEMENT OF ASSESSMENT BY COMMISSIONER MORE THAN ONE YEAR AFTER ASSESSMENT BY INCOME-TAX OFFICER—LEGALITY—INCOME 'ESCAPING ASSESSMENT' MEANING OF—APPEAL TO COMMISSIONER—POWER OF COMMISSIONER TO ENHANCE ASSESSMENT—HISTORY OF PREVIOUS YEARS HOW FAR RELEVANT—INDIAN INCOME TAX ACT (XI OF 1922), SECS. 32, 33, 34.

In his return of income for the year 1932-33 the assessee showed his gross income from the sales of jewellery at Rs. 26,553. The Income Tax Officer accepted these figures and applying a certain rate of profit made an assessment on July 22, 1933. The Assistant Commissioner dismissed the assessee's appeal and enhanced the assessment by a certain sum on October 31, 1933. The assessee appealed to the Commissioner who dismissed the appeal on September 3, 1934. On the same day the Commissioner issued a notice to the assessee under Section 33 to show cause against enhancement and on October 8, passed an order enhancing the

income from sales of jewellery to Rs 50,000 from Rs. 26,553. On a reference by the Commissioner of Income Tax:

Held, (1) *That the sum of Rs. 23,447 must be regarded as income which had escaped assessment within the meaning of Section 34 of the Income Tax Act and, as no notice was issued to the assessee within one year of 31st March 1933, the Commissioner was not entitled to enhance the income from Rs. 26,553 to Rs. 50,000; (2) that the Commissioner was not justified in enhancing the assessment to Rs. 50,000 merely because of the history of the previous years or because the expenditure was very high compared with the extent of trade.*

The decision of the Privy Council in Rajendranath Mukherjee's case *(61 Cal. 285) does not justify an inference that an assessment is not concluded when the amount of tax payable by the assessee had been determined by the Income Tax Officer and a demand notice issued to him. Proceedings after the issue of the demand notice do not form part of the assessment.*

The Commissioner can take action under Section 33 and proceed to enhance the assessment after disposing of an appeal under Section 32; but the exercise of the powers of review under Section 33 are subject to the limitation provided in Section 34.

The Commissioner when dealing with an appeal under Section 32 can pass orders only with respect to the subject matter of the appeal. He cannot suo motu *proceed to enhance the assessment which he has power to do under Section 33.*

The history of the assessment of the previous years is irrelevant for the purpose of determining whether the sales have been understated during the assessment year and the fact that the expenses in relation to the disclosed extent of trade were high is not sufficient material for finding that a number of sales were omitted from the account books of the assessee.

Sec. 34 is not confined to cases where income has 'eluded notice,' but includes cases where income has been returned but has not been assessed.

Cases referred to:

JESA RAM *v.* COMMISSIONER OF INCOME TAX, PUNJAB, [1921] (I.L.R. 8 Lah. 347; 101 I.C. 129; A.I.R. 1921 Lah. 421; 2 I.T.C. 342).

MADAN MOHAN LAL v. COMMISSIONER OF INCOME TAX, DELHI (1935) (3 I T.R. 438; I.L.R. 16 Lah. 937; 158 I.C. 718; A.I.R. 1935 Lah. 570).

RAJENDRANATH MUKHERJEE v. COMMISSIONER OF INCOME TAX, BENGAL (1934) 2 I.T.R. 71; I.L.R. 61 Cal. 285; 66 M.L.J. 121; A.I.R. 1934 P.C. 30.

Case stated by the Commissioner of Income Tax, Punjab, N.W.F.P. and Delhi under Sec. 66 (2) of the Indian Income Tax Act in the matter of the assessment of Messrs. Nawal Kishore Kharaiti Lal of Delhi for the year 1932-1933. [Case No. 19 of 1935].

The facts are fully stated in the Judgment.

Mehar Chand Mahajan and *Bhagwat Dyal*, for the assessee.

J. N. Aggarwal and *S. M. Sikri*, for the Commissioner of Income Tax.

JUDGMENT.

Under Section 66 (2) of the Indian Income tax Act, the Commissioner of Income-tax, Punjab, has referred the following questions of law, arising out of the assessment for the year 1932-33 on Messrs. Nawal Kishore Kharaiti Lal to this court :—

(1) Was there any material upon which the Commissioner could determine as fact that the assessee's Agra jewellery accounts were not true and complete, that his Delhi jewellery account of the relevant sales, and that the Income-tax Officer's estimate of the profits of the said Delhi jewellery business was below the actual profits?

(2) Was the Commissioner's determination in respect of 1932-1933 assessment barred by time at the date of the order, 8th October 1934, by the provisions of Section 34?

By its order dated the 11th of June 1935, this court directed the Commissioner of Income-tax, Punjab, to state the case on the following further question of law :—

(3) Whether the Commissioner could take action under Section 33 and proceed to enhance the assessment, after having disposed of the assessee's appeal under Section 32 of the Income-tax Act?

The assessee is known as the leading wholesale jeweller in Delhi running a business that has been in existence for over a

hundred years. For the year 1932-33 the assessee was assessed on a total income of Rs. 18,494, under Section 23 (3) of the Act. The assessment order was passed by the Income Tax Officer on the 22nd of July, 1933. In his return the assessee had shown his gross income from the sales of jewellery at Rs. 26,553. He had also shown an income of Rs. 4,724 from the sales of precious stones The Income tax Officer accepted these figures so far as the sales of jewellery and precious stones were concerned. He was, however, of the opinion that the flat rates of 10 per cent. and 5 per cent. profits respectively applied by the assessee were too low, and as there was no proof in support of these rates, he applied the rates of 20 per cent. and 15 per cent. profits respectively regarding jewellery sales and sales of precious stones. The Income-tax Officer thus accepted the correctness of the assessee's accounts so far as sales were concerned but enhanced the rates of profit applicable to the sales. Against this assessment the assessee preferred an appeal to the Assistant Commissioner of Income-tax. The Assistant Commissioner served on the assessee a notice under Section 31 of the Act to show cause why certain items of expenditure which had been allowed, by the Income-tax Officer should not be disallowed and the income enhanced by this amount. By means of his order dated the 31st of October 1933, the Assistant Commissioner of Income tax dismissed the assessee's appeal, and then enhanced the assessment by a sum of Rs. 4,512. The Income-tax Officer had allowed the assessee Rs. 1,099 as motor car expenses relating to the Agra Branch and Rs. 1,588 as motor car expenses relating to the Delhi shop. Both these items were disallowed by the Assistant Commissioner of Income-tax. Rs. 1,825 had been allowed by the Income-tax Officer as expenses of litigation with respect to certain suits. This sum was also disallowed by the Assistant Commissioner. The enhancement thus consisted of the disallowance of certain expense items which had been allowed by the Income-tax Officer.

Against the order enhancing the assessment, the assessee preferred an appeal to the Commissioner of Income-tax under Section 32 of the Act. The Commissioner partially accepted this appeal in so far as to allow Rs. 200 as motor car expenses for the Agra Branch and Rs. 500 for the Delhi shop. In other respects this appeal was dismissed by the Commissioner by his order,

dated the 3rd of September, 1934. It appears that on the same date the Commissioner of Income-tax issued a notice to the assessee under Section 33 of the Act to show cause against enhancement so far as his income from sales of jewellery was concerned. On the 8th of October 1934, the Commissioner of Income-tax passed an order in exercise of his power of review under Section 33, and enhanced the income from sales of jewellery to Rs. 50,000 from Rs. 26,553. This reference is mainly concerned with the questions of law arising out of the enhancement alluded to above. As mentioned above the books of the assessee show Rs. 26,553 as income from sales of jewellery. The Income-tax Officer had accepted his figure as correctly representing 'sales of jewellery' by his order dated the 22nd of July 1933. The Commissioner of Income-tax, by his order dated the 8th October, 1934, raised this figure to Rs. 50,000.

The first question for determination is whether the sum of Rs. 23,447 (being the difference between Rs. 50,000 and Rs. 26,553) can be regarded as income which had "escaped assessment" within the purview of Section 34 of the Act. The Commissioner was of the opinion that the sales were greatly under-stated at both the Agra and the Delhi shops and that the sales total was not, therefore, complete and true in fact. The meaning of the Commissioner appears to be that a number of sales were not entered in the account books of the assessee and thus the sum of Rs. 26,553 did not represent the total amount realized by the assessee. It was contended by the learned counsel for the assessee that in the circumstances alluded to above the sum of Rs. 23,447 must be regarded as income which had 'escaped assessment' during the year 1932-33 and that as no notice was served on the assessee within one year of the end of the assessment year the Commissioner could not proceed to re-assess such income in view of the provisions of Section 34 of the Act. Reference may be made in this connexion to a Full Bench ruling of this Court reported as I. L. R. 16 Lah. 937 (*Madan Mohan Lal* v. *Commissioner of Income Tax, Delhi*). The facts of that case were as follows :—" The assessee M. M. L. had to be assessed both as an individual and as a *karta* of a joint Hindu family. He made a return in his personal capacity in which he included an item of Rs. 79,543 as personal income. He also made a return on behalf

of the joint Hindu family and the Income-tax Officer who was dealing with that income made an assessment thereon, including the item of Rs. 79,543. Thereupon the Income-tax Officer, who was dealing with the assessment of M. M. L. as an individual assessed him on the return furnished by him, but excluding the item of Rs. 79,543 on the ground that it had been assessed as income of the joint family by the Officer dealing with that case. On appeal in the joint family case the Assistant Commissioner accepted the appeal and excluded the item of Rs. 79,543 from the income of the joint family holding that it was the personal income of the assessee. The Income-tax Officer dealing with the personal case then took action under Section 34 of the Act and decided that the item of Rs. 79,543 had "escaped assessment" and, accepting the return of the assessee, assessed him on this item. The assessee objected that Section 34 had no application, that the income had not escaped assessment and that the fresh assessment was without jurisdiction." It was held by ADDISON, A. C. J., that the sum of Rs. 79,543 did "escape assessment" in the hands of the assessee at first, if these words are given their ordinary meaning and that there was no reason to give the words "escaped assessment" some restricted meaning. DIN MOHAMMAD, J., was of the opinion that Section 34 is not confined to cases where the income in question is not disclosed in the return, that if an item of income is included in the return submitted by an assessee during the tax year, but is left unassessed by the Income-tax Officer or if assessed in the first instance, the assessment is cancelled by an appellate or revisional authority such income "escaped assessment" within the meaning of Section 34. DALIP SINGH, J., dissented from the opinion of the other learned Judges and held that the word 'escape' was not to be read in the widest sense that that word was capable of bearing, and that the word 'escaped' was equivalent to "eluded notice" in the course of assessment and did not mean 'had avoided being assessed.' In coming to this conclusion the learned Judge relied on the Privy Council ruling reported as I. L. R. 61 Cal. 285 (*Rajendranath Mukherjee* v. *Commissioner of Income-tax, Bengal*). I respectfully agree with the opinion of the majority so far as the meaning of the words "escaped assessment" is concerned. It appears to me, however, that in the present case the sum of

Rs. 23,447 must be held to be income which had "escaped assessment" even if the words "escaped assessment" are used in the restricted sense as being equivalent to "eluded notice." The books of the firm showed income from the sales of jewellery as Rs. 26,553 while the Commissioner computed the income from that source as being Rs. 50,000. The difference between the two incomes did not find any place either in the return or in the books of the company. In the every nature of things, therefore, this income was bound to "elude notice" and did "elude notice."

The Commissioner has stated that the enhancement made by him did not amount to the assessing of something that had "escaped assessment." According to him he had merely "enhanced the existing determinations of the self-same subject," and had discovered no new source or new income that had "escaped," that the same profits from the same sources stood, but the "determination of their quanta was revised wholly upon existing record." I am unable to appreciate the force of these observations of the Commissioner. The order passed by the Commissioner under Section 33 of the Act shows that he estimated the income from the sales of jewellery to be Rs. 50,000 instead of Rs. 26,553, as according to him the sales were greatly under-stated and the sales total was not therefore complete. The enhancement to Rs. 50,000 clearly implies that sales to the extent of Rs. 23,447 were estimated to have taken place but were not included in the books of the assessee. The sales which had been omitted from the account books of the assessee had obviously "escaped assessment" when the Income-tax Officer passed the order of assessment. These sales therefore clearly fall within the meaning of the words "income that had escaped assessment" according to the decision of the Full Bench in *Madan Mohan Lal* v. *Commissioner of Income Tax, Delhi.*

The learned counsel for the Commissioner, however, contends that the word "assessment" was not synonymous with the "order of assessment" that assessment was a continuous process and included proceedings before the Income-tax Officer, the Assistant Commissioner, the Commissioner and even the High Court in cases where a reference was made to that Court, and that in this view of the matter the assessment for 1932-33 had not been concluded when the Commissioner enhanced the income

derived from sales of jewellery from Rs. 26,553 to Rs. 50,000. It was urged that as the assessment had not been completed no income had yet "escaped assessment", and that the provisions of Section 34 of the Act were therefore, inapplicable in the present case. Reliance was placed in this connection on a Privy Council ruling reported as *Rajendranath Mukherjee* v. *Commissioner of Income-tax, Bengal* (I.L.R. 61 Calcutta 285), where it was held that "so long as proceedings for the assessment of an assessee's income for a financial year are pending, no final assessment having been made upon him, his income has not 'escaped assessment' within the meaning of Section 34 of the Indian Income-tax Act, 1922, so as to make service of a notice within one year of the end of the year, as therein required a condition to assessment. Where a case does not fall within Section 34, an assessment can be made at any time under Section 23, sub-section (1), pursuant to a notice under Section 22, sub-section (2) calling for a return". The observations of their Lordships of the Privy Council must, however, be read subject to the facts of the case which was under consideration by their Lordships at the time of making the observations quoted above. It is, therefore, necessary to make a detailed reference to the facts of that case which were as follows:—"Towards the end of year 1926-27, the partners of the registered firm of Martin & Co., which also carried on business in Calcutta, purchased the business and assets of Burn & Co. The purchase was effected not by or on behalf of the firm of Martin & Co., but by the partners of that firm as individuals who contributed funds for the purpose proportionally to their shares in Martin & Co., and became partners in Burn & Co., with the same shares therein as they held in Martin & Co. In the year 1927-28 Martin & Co., was a registered firm, while Burn & Co., was unregistered. On the 7th April 1927, the Income-tax Officer of District I issued a notice to Burn & Co., under Section 22 (2) calling for a return of their total income for the year to the 31st March 1927, with a view to assessing them for the year 1927-28. A similar notice was issued to Martin & Co., on the 8th April 1927, by the Income-tax Officer of District II. When they issued these separate notices, the Income-tax Officers were unaware that the business of Burn & Co., had been bought by the partners of Martin & Co., on the 24th September 1927,

Martin & Co., made a return of their total income in compliance with the notice issued to them in April, and on the 13th January 1928, Burn & Co., made their return. Meantime, the purchase of the business of Burn & Co., by the partners of Martin & Co., having come to the knowledge of the income-tax authorities, Burn & Co.'s file was transferred to the Officer dealing with District II and on the 25th February 1928, he made an assessment on Martin & Co., in respect of the combined incomes returned by Martin & Co., and Burn & Co., on the footing that the business of Burn & Co., had become a branch of the business of Martin & Co. Martin & Co., appealed against this assessment and ultimately the income of Burn & Co., was excluded from the return of Martin & Co. Thereafter on the 8th of November 1930, an assessment was made on Burn & Co., on their income as returned by them on the 13th of January 1928."

It was in these circumstances that their Lordships held that the income of Burn & Co., had not " escaped assessment ", as no final assessment had ever been made on Burn & Co.

The learned counsel for the Commissioner relied on the following observation in the judgment of their Lordships of the Privy Council: " That the word 'assessment' is not confined in the statute to the definite act of making an order of assessment appears from Section 66 which refers to " the course of any assessment." It must, however, be remembered that this observation was made by their Lordships to repel the contention raised on behalf of the appellant to the effect that assessment is a definite act and that if an assessment is not made on income within the tax year, then that income has " escaped assessment " within that year and can be subsequently assessed only under Section 34 within its time limitation. In that case no order of assessment had ever been made against Burn & Co., and their income had at one time been included in the income of Martin & Co., and thereafter excluded from such assessment. What was really decided in that case was that an assessment can be made under Section 23 (1) of the Act more than a year, in fact at any time, after the assessment year, if in the meantime no final assessment has been made. *Rajendranath Mukherjee* v. *Commissioner of Income-tax, Bengal*, does not justify an inference that an assessment is not concluded when the amount of tax payable

by the assessee has been determined and a demand notice issued to him. The use of the words 'cancel the assessment', 'make a fresh assessment', and "annul or enhance the assessment", in Sections 27, 30 and 31 shows that the proceedings after the issue of the demand notice do not form part of the assessment. I would, therefore, hold that the sum of Rs. 23,447 must be regarded as income which had "escaped assessment" within the purview of Section 34 of the Act, and that such income could only be re-assessed if a notice had been issued to the assessee within one year of the 31st of March, 1933. In the present case no notice was issued to the assessee till the 3rd of September, 1934, and the Commissioner was therefore not entitled to enhance the income from Rs. 26,553 to Rs. 50,000. I would accordingly answer the second question referred by the Commissioner in the affirmative.

On the third question I am of the opinion that the Commissioner could take action under Section 33 and proceed to enhance the assessment after having disposed of the assessee's appeal under Section 32. The exercise of the powers of review under Section 33 would, however, be subject to the limitation provided in Section 34, as held in *Jesaram* v. *Commissioner of Income-tax, Punjab* (I. L. R. 8 Lahore 347). The learned counsel for the assessee contended that the provisions of Section 32 (3) of the Act give the Commissioner ample powers when disposing of an appeal to pass such orders as he thinks fit and that this includes the power to enhance an assessment. The use of the word "thereon" in this sub-section, however, seems to imply that the Commissioner when dealing with the appeal under Section 32 can pass orders only with respect to the subject matter of the appeal, and cannot, *suo motu*, proceed to enhance an assessment which he has the power to do under Section 33 of the Act. If the Commissioner calls for the records of a case after disposing of the appeal preferred to him against the order of an Assistant Commissioner he would be exercising powers of review in respect of proceedings which have been taken by an authority subordinate to him and not in respect of proceedings taken by himself as a court of appeal. I would, therefore, answer the third question in the affirmative.

In view of the findings given above, the first question is not

of any great importance. The only material referred to by the learned counsel for the Commissioner consists of the history of the assessee's relations with Banji Lal and of the history of his assessment for several years in the past. There is no evidence to show that the assessee was falsifying the accounts for the year under assessment. The Commissioner has also remarked in his referring order that he was struck by the surprising relation of the expenditure to the disclosed extent of trade. The history of the assessment of the previous years is irrelevant for the purpose of determining whether the sales have been understated during the assessment year. The fact that the expenses of the Delhi shop in relation to the disclosed extent of trade were rather high cannot be held to provide any material for the finding that the sales total was not complete and that a number of sales amounting to Rs. 23,447 were omitted from the account books of the assessee. I would, therefore, answer the first question in the negative. The Commissioner will pay the costs of the assessee which we fix at Rs. 100 (One hundred).

Reference answered accordingly.

[IN THE LAHORE HIGH COURT.]

HAVELI SHAH SARDARI LAL

v.

COMMISSIONER OF INCOME TAX, PUNJAB.

SIR JAMES ADDISON AND ABDUL RASHID, JJ.

May 6, 1936.

INTEREST ON SECURITIES—SALE OF SECURITIES—INTEREST UP TO DATE OF SALE PAID TO VENDOR WHETHER DEDUCTABLE IN ASSESSING PURCHASER—INDIAN INCOME TAX ACT (XI OF 1922), SEC. 8.

Interest on Government securities does not accrue from day to day but on certain fixed days and, where securities are purchased at a price expressed as a capital sum plus interest computed de die in diem *from the last due date to the date of sale, interest*

thus paid to the vendor is not deductable from the interest actually received by the purchaser on the next due date, in assessing the purchaser under Sec. 8 of the Indian Income Tax Act.

The mere quotation in the bargain, of estimated accrued interest, does not establish a separate contract in respect of the interest, and even if it were considered to be a separate contract, it would remain part and parcel of the whole purchase consideration and would not be deductable.

Cases referred to:

COMMISSIONERS OF INLAND REVENUE *v.* OAKLEY [1925] (9 TAX CAS. 582; 41 T.L.R. 568).

RANJIT PRASAD SINGH *v.* COMMISSIONER OF INCOME TAX, BIHAR AND ORISSA [1930] (4 I. T. C. 264; 9 Pat. 194; 123 I. C. 617; A. I. R. 1930 Pat. 33).

WIGMORE *v.* THOMAS SUMMERSON AND SONS LTD. [1925] (9 Tax Cas. 577; 41 T.L.R. 568).

Case stated by the Commissioner of Income Tax, Punjab, N. W. F. P. and Delhi, under Sec. 66 (2) of the Indian Income Tax Act in the matter of the assessment of Messrs. Haveli Shah, Sardari Lal of Dinga for the year 1934-35. [Civil Reference No. 13 of 1936].

M. L. Puri and *V. N. Sethi* for the assessees.

Sarva Mitra Sikri for *Jagan Nath Aggarwal*, for the Commissioner of Income tax.

ORDER.

This is a reference by the Commissioner of Income-tax regarding the assessment of a joint Hindu family Haveli Shah Sardari Lal for the assessment year 1934-35. The question of law referred is as follows:—

"The assessee (not being a dealer in securities by way of "business") having purchased securities at a price expressed as a capital sum plus interest computed *de die in diem* from the last due-interest-date to date of purchase, is the said computed interest deductable from the interest actually received by him, in assessment under section 8 of the Act?"

The assessment in question was made on a total income of Rs. 3,00,099 including Rs. 2,68,785 under section 8 of the Income tax Act. The latter sum is made up as follows :—

Interest (gross) received from Government in respect of securities purchased 1926-32 ...	2,55,750	0	0
Interest (income-tax free) received in respect of securities purchased from April to November 1933 ...	13,035	0	0
Total ...	2,68,785	0	0

From this sum the assessee wishes to take the sum of Rs. 9,102-1-4 on the ground that it was interest paid by him to the sellers of the securities at the time of the 1933 purchases. These purchases consisted entirely of Government of India 1945-55 (income-tax free) 5 per cent loan. Ordinary income-tax was thus not charged under section 8, 2nd proviso, but in accordance with section 16 (1) super-tax is chargeable on the whole sum and was charged upon Rs. 2,68,785. The sole question is whether the sum of Rs. 9,102-1-4 should be deducted from charge.

The Commissioner has stated that no precise evidence of the terms of purchase was given except to the extent of putting in advices from the purchasing brokers of Banks in Calcutta, and he has given the following as an example :—

"In accordance with the instructions contained in your letter I beg to advise the purchase of securities as detailed below in further execution of your order :—

"P. No. 2267.

"To cost of 5 per cent. loan 1945-55 for rupees 16,500 at Rs. 106-14-0 per cent. ...	17,634	0	0
"Interest from 15th April 1932 to 12th October 1932, being five months and 27 days	405	10	0
"Commission at ¼ per cent. on Rs. 18,040 ...	45	4	0
"Postage, etc. ...	0	11	0
Debited to your account Rs.	18,085	15	0

The Commissioner has stated that so far as appears the amount of Rs. 9,102-1-4 is wholly comprised of the computed interest. We are not concerned with the past practice of the Income-tax authorities. Section 8 makes income-tax payable by an assessee under the head 'Interest on securities' in respect of the interest *receivable* by him on any security of the Government of India etc. This section can only have one meaning and that is that income-tax is payable on the interest receivable from Government by any holder of such a security. This was the view taken by a Special Bench of the Patna High Court in *Ranjit Prasad Singh* v. *Commissioner of Income Tax, Bihar and Orissa.* There the opinion was expressed that section 8 of the Income-tax Act was conclusive so far as this question was concerned. The interest, it was said, was undoubtedly receivable by the assessees. It was received by them and the section thus made them liable. It was pointed out that interest on Government securities did not accrue from day to day but on certain specified dates. It did not, therefore, accrue to the vendors at all since they sold before any interest accrued. The form the contract took and the terms in which it was expressed were matters between the assessees and the vendors, and the assessees might well have protected themselves by insisting that the amount of tax which would ultimately be payable by them under section 8 should be deducted from the purchase money.

The Commissioner of Income Tax is in agreement with this decision and has given his opinion that the computed interest was part of the purchase price and was not in any event deductable from the assessee who actually received interest. He, however, referred the question to this court as it has not been agitated so far here.

In my judgment the machinery sections of the Act also help in determining this matter though I am of the same opinion as was held by the learned Judges in the case quoted that the contention of the assessee must fail on the terms of section 8 of the Act, as no interest was receivable or could be received until the due date, by which time the assessee was owner and received the whole interest. Again, it would be impossible to keep track of interest adjustments between transferors of negotiable securities. Section 18 (3) requires that ordinary income-tax (when due) shall

be deducted at the time of the payment while Section 18 (5) provides that any such deduction shall be treated as a payment of income-tax on behalf of the owner of the security and credit shall be given to him therefore in the assessment, if any, made for the following year. Lastly, Section 48 (3) provides for refund of the excess so credited to the owner of the security, if in the event the due charge is less than the deduction. The credit, therefore, under Section 18 (5) can only be allowed to the owner of the security on his producing the certificate necessary under Rule 38 while it is impossible to consider computed interest in the hands of the vendors. These machinery sections, therefore, support the view that the tax is chargeable only on the owner of the security at the time when the interest becomes receivable.

The same question has arisen in England and is fully discussed in *Wigmore* v. *Thomas Summerson and Sons Ltd.* (9 Tax Cas. 577) as well as in *Commissioners of Inland Revenue* v *Oakley* (9 Tax Cases 582) by ROWLATT, J. In the first case the stock sold was not sold with an allowance for computed interest but *en bloc*. But that does not make any difference. ROWLATT, J., made the following pertinent remarks in the first named case :—

"To my mind it is absurd to say that a person is paying £ 5,000 in March for £ 5,000 to be paid in June. He does not do it. Therefore there would have to be, in any case, a valuation of the amount of accrued interest that has been sold, The truth of the matter is that the seller does not receive 'interest' while it is interest that is the subject matter of taxation. He receives the price of the expectancy of interest and that is not the subject of taxation, and the whole thing, I think, really depends upon that fallacy."

In the second case the same learned Judge pointed out that the results might be curious but many results in super-tax were curious. He goes on to say :

"The result is that nobody on the super-tax level, who has not more money (?) than appreciation of income-tax law will ever buy a security that is full of dividend because he is buying super-tax ; and if a man wants to sell a security, if he is on the super-tax level he had better sell when it is full of dividend, because then he is selling super-tax. These are accidents which do not seem to me possibly to affect the administration of the Act, and

I cannot conceive how the Acts could be administered, except at great cost and inconvenience not only to the Revenue but to private people who now are not concerned with these minutiae, if the contention which the Crown put forward here, not in their own interest but in the interest of purchasers really, was to succeed."

The last observation of ROWLATT, J., has already been alluded to by me when dealing with the machinery sections. Clearly it would be impossible to keep track of interest adjustments between transferors and transferees of negotiable securities and a statute, as remarked by DUNEDIN, L.J., in *Whitney* v. *Commissioners of Inland Revenue* (10 T.C. at page 110) is designed to be workable and the interpretation thereof by a court should be to secure that subject. I have no hesitation in holding that Section 8 itself is conclusive on the matter while the machinery sections make it still more clear.

The only contention remaining to be further discussed is that because the purchase price was expressed separating a computed accrual of interest, that amount was not in fact a part of the purchase consideration, but was a separate charge incurred against the interest when the assessee eventually received it. This argument has already been dealt with by ROWLATT, J., and it seems clear that the mere quotation in the bargain of estimated accrued interest does not establish a separate contract in respect of the interest, and even if it were considered to be a separate contract, it would remain part and parcel of the whole purchase consideration, and would not be deductable.

I would, therefore, answer the question put in the terms of the Commissioner's opinion already given. There will be no order as to costs.

Reference answered accordingly.

[IN THE LAHORE HIGH COURT.]

BADRI SHAH SOHAN LAL
v.
COMMISSIONER OF INCOME TAX, PUNJAB & N. W. F. P.

SIR JAMES ADDISON AND ABDUL RASHID, JJ.

June 11, 1936.

MONEYLENDING BUSINESS—PURCHASE OF DEBTOR'S PROPERTY PENDING INSOLVENCY OF DEBTOR FOR SUM EXCEEDING DEBT—PURCHASER ORDERED TO RANK AS UNSECURED CREDITOR AS REGARDS EXCESS PAID—LOSS INCURRED, WHETHER LOSS IN BUSINESS OR CAPITAL LOSS—INDIAN INCOME TAX ACT (XI OF 1922), SECS. 24, 10 (2) (ix).

During the pendency of insolvency proceedings against a firm, the assessee who was a money lender and one of the creditors of the firm purchased property from the firm for Rs. 18,000. He paid Rs. 9,497 and adjusted the balance, namely Rs. 18,503 towards the debt due to him. The Insolvency Court converted the sale into a mortgage for Rs. 8,500 and ordered that the assessee should rank as an unsecured creditor for the balance of Rs. 9,497. The assessee got only Rs. 3,097 from the official receiver towards this unsecured debt and claimed that the deficit of Rs. 6,403 should be deducted from the profits earned by him on the ground that it was a loss incurred in his money lending business : Held, *that the purchase of the land to the extent of Rs. 9,497 did not arise out of the assessee's monylending business and the loss suffered by him in respect of this purchase cannot be regarded as expenditure incurred solely for the purpose of earning profts or gains in the moneylending. Section 24 of the Indian Income tax Act was also not applicable to the case and the claim could not be allowed.*

Case stated by the Commissioner of Income-tax, Punjab, N.W.F.P. and Delhi under Sec. 66 (2) of the Indian Income-tax Act (XI of 1922) in the matter of the assessment of Messrs. Badri Shah Sohan Lal for the year 1934-35. [Civil Reference No. 4 of 1936].

Kirpa Ram Bajaj, for the Assessee.

J. N. Aggarwal and *M. M. Aslam Khan*, for the Commissioner.

ORDER OF THE HIGH COURT.

SIR JAMES ADDISON.—The Commissioner of Income-tax Punjab, has referred the following questions of law for the decision of this Court under Section 66 (2) of the Indian Income-tax Act:—

"The assessee having purchased from his debtor a piece of land for the amount of debt, plus further Rs. 9,497, a deficit of Rs. 6,403 having subsequently materialised in respect of that Rs. 9,497 by reason of decree which converted the purchase into mortgage for the original debt, and ranked the above balance with unsecured debts of the debtor declared insolvent: is the deficit to be set off against the assessed profits, whether as expenditure under section (10) (2) (ix) read with section 13, or as loss of profits under Section 24 of the Act".

The assessee is a bullion dealer and money lender of Gujranwala. In 1934-35 he was assessed on a total income of Rs. 20,549 out of which Rs. 14,673 represented his profit in business. Rs. 8,503 were due from Messrs. Shiv Dayal Amin Chand to the assessee in May 1928. The debtors sold their land for a sum of Rs. 18,000 to the assessee on the 28th of May 1928. This sum of Rs. 18,000 was made up of Rs. 8,503 due from the vendors to the vendee, and an advance of Rs. 9,497 made by the vendee to the vendors. The assessee paid this sum in cash to Messrs. Shiv Dayal Amin Chand. At the time of this sale however insolvency proceedings were pending against Amin Chand-Shiv Dayal. On the 5th of October 1931, the learned District Judge passed an order converting the above mentioned sale into a mortgage without possession for Rs. 8,500. As regards the balance of Rs. 9,497 the learned District Judge ordered that the assessee shall rank as unsecured creditor and shall have to prove him claim. Up to May 1933, the assessee received from the Official Receiver the amount of the original debt amounting to Rs. 8,503 and interest thereon and a further sum of Rs. 3,097 leaving a deficit of Rs. 6,403. This is the sum which the assessee seeks to deduct from the profits earned by him during the years of assessment.

The learned counsel for the assessee contended that the assessee had bought the land belonging to Shiv Dayal-Amin Chand for Rs. 18,000 in order to secure payment of his debt amounting to Rs. 8,503 and that the whole transaction of sale must, therefore, be regarded as a transaction arising out of the money lending business carried on by the assessee. In our opinion this contention is wholly devoid of force. Purchase of lands was not the business of the assessee. If he merely wanted to obtain payment of the debt due to him from the vendors he could have purchased a part of the land belonging to the vendors for a sum of Rs. 8,503. It was not necessary for him in order to realise his loan to purchase a large area of land for a sum of Rs. 18,000. The transaction of the purchase of land is really divisible into two transactions, that is, a purchase of a part of the land for Rs. 8,503 in order to secure the payment of the loan due to the assessee, and a purchase of another part of the land for Rs. 9,497 as an independent purchase of landed property. The entire sum of Rs. 8,503 due to the assessee in respect of money-lending has been paid by the Official Receiver to the assessee. The purchase of a part of the land for Rs. 9,497 did not arise out of the money-lending business and any loss suffered by the assessee in respect of this purchase cannot be regarded as expenditure incurred solely for the purposes of earning profits or gain in money-lending business. Section 24 of the Income-tax Act has also no applicability to the facts of the present case.

For the reasons given above we hold that the loss of Rs. 6,403 incurred by the assessee as a result of the purchase of land by him was not deductable from profits under any provision of the Indian Income-tax Act. We consequently answer the question referred to us in the negative. The assessee shall pay the costs of the Commissioner.

Reference answered in the negative.

[IN THE LAHORE HIGH COURT.]

MACNABB

v.

COMMISSIONER OF INCOME TAX, PUNJAB.

SIR JAMES ADDISON AND ABDUL RASHID, JJ.

March 18, 1936.

BUSINESS EXPENDITURE—INTEREST ON MONEY BORROWED IN BRITISH INDIA FOR PURCHASING SECURITIES OUTSIDE BRITISH INDIA--WHETHER DEDUCTABLE FROM INCOME TAXABLE IN BRITISH INDIA—INTEREST—OVERDRAFT ON SECURITY OF FIXED DEPOSIT—INTEREST ON OVERDRAFT, WHETHER DEDUCTABLE FROM INTEREST ON FIXED DEPOSIT—INDIAN INCOME TAX ACT (XI OF 1922), SECTION 10 (2) (iii).

Interest paid on sums borrowed in British India to purchase sterling securities which are retained and the income from which is received outside British India, has to be treated as a charge on the interest from those securities which is not liable to Indian income-tax and is not deductable under Section 10 (2) (iii) of the Indian Income Tax Act from the other income of the assessee liable to tax in British India.

The assessee, a civil servant, whose main source of income was his salary deposited Rs. 74,000 on fixed deposit with a bank. He borrowed Rs. 66,000 from the bank on the security of the fixed deposit and purchased certain shares in England, the dividends from which were payable in England, and not taxable in India. The assessee claimed that in calculating his assessable income he was entitled to set off the interest which he had to pay to the bank on the loan against the interest payable to him by the bank on the fixed deposit: Held *(1) that the assessee was not entitled to the deduction claimed as he did not carry on any business and Sec. 10 (2) (iii) had no application: (2) that even assuming he was engaged in a foreign business, as the amount was borrowed for purchasing securities outside British India and the interest on the securities was payable outside British India, the interest on the amount borrowed could not be deducted from his income taxable in British India.*

Cases refered to and followed :

COMMISSIONER OF INCOME TAX, MADRAS v. SOMASUNDARAM CHETTIAR [1928] (109 I.C. 369; 54 M.L.J. 436; A.I.R. 1928 Mad. 487; 2 I.T.C. 505).

PROVIDENT INVESTMENT CO., *In re* [1932] (1932 Comp. Cas. 312; 135 I.C. 810; 6 I.T.C. 21).

Case stated by the Commissioner of Income Tax, Punjab, N.W.F.P., and Delhi, under Sec. 66 (2) of the Indian Income Tax Act (XI of 1922) in the matter of assessment of Mr. A.C. Macnabb, I.C.S., Deputy Commissioner of Attock, for the year 1933-1934 [Civil Ref. No. 1 of 1936].

The necessary facts are stated in the judgment.

H. J. Rustomji, for the assessee.

J. N. Aggarwal, for the Commissioner.

JUDGMENT.—The following question of law has been referred for the opinion of this Court by the Commissioner of Income Tax, Punjab :—

"The assessee having incurred expenditure by way of interest upon monies borrowed for the purposes of foreign investments, was that expenditure to be deducted from his income assessed in British India, the said income comprising or including interest income paid on a fixed deposit by the same Bank?"

The facts are simple. The assessee is a civil servant whose main source of income is salary. In 1929 and 1930 he deposited with the Sargodha Central Co-operative Bank sums on fixed deposit, aggregating Rs. 74,000/-, on which he was paid interest at the rate of 7½ per cent per annum. In October 1930 he wished to purchase industrial shares etc. in England. The fixed deposits were not mature and he borrowed from the same Bank Rs. 66,600/- which he converted into sterling and remitted to England. The assessee cannot be said to be engaged in the business of stock-dealing nor could he engage in such. The dividends, etc., derived from his investments in England, were not taxable in India. In the assessment year in question he earned a certain sum as interest on his fixed deposits and he had to pay certain sum as interest on the overdraft, the latter sum being slightly less than the former. His claim is that he is entitled to set off the interest on

his over-draft against the interest on his fixed deposits on which the Bank had a lien in consequence of the overdraft granted to him.

Even if it be presumed that he was engaged on a foreign business there is authority for the view that the interest paid on sums borrowed in British India to purchase sterling securities, retaining those securities and the interest therefrom outside British India, has to be treated as a charge on the interest from those securities which are not liable to Indian income-tax and is not deductable under Section 10 (2) (iii) of the Income-tax Act from the other income of the assessee liable to tax as accruing and arising in British India. This was laid down in *Provident Investment Co., In re* by a Bench of the Bombay High Court and there is a similar decision by the Madras High Court reported in *Commissioner of Income Tax v. Somasundaram Chettiar*. The only distinction between the two cases is that in the later case the business in India had a Branch in the Federated Malay States while in the former case the Indian business was purchsing securities outside British India through bankers or brokers in Bombay. In both the cases it was held that the interest payable on the borrowed sums for the foreign business could not be deducted from the other income.

The case of the assessee before us is even worse as it cannot be held that he is carrying on business. All that he did was to raise capital in British India to invest it outside British India and the interest he had to pay on the borrowed capital was an expense incurred in connection with his outside investment and had nothing to do with anything else. It is only in case he is carrying on business that such a deduction can be claimed and from the authorities quoted it is clear that the borrowing must be for the purpose of carrying on a business the profits of which accrue in British India. The paragraph in the Income-tax Manual relied upon by the assessee in no way helps him.

For the reasons given we answer the question in the negative and allow the Commissioner of Income Tax his costs.

[IN THE MADRAS HIGH COURT.]

CHIDAMBARAM CHETTIAR

v.

COMMISSIONER OF INCOME TAX, MADRAS.

MADHAVAN NAIR, STONE AND KING, JJ.

September 18, 1935.

FOREIGN BUSINESS—CONSTRUCTIVE REMITTANCE—PAYMENT OUTSIDE BRITISH INDIA OF ADVANCE FOR PURCHASE OF LAND IN BRITISH INDIA—SALE COMPLETED LATER—DATE OF REMITTANCE, WHETHER DATE OF ADVANCE OR DATE OF COMPLETION OF SALE.

The assessee, a Nattukottai Chetti who carried on business at Klang(in Burma) entered into an agreement with one S. A. Rm. who carried on business at Penang for the purchase of a house site belonging to S. A. Rm. in British India. On the 3rd April 1929, a sum of Rs. 50,000 was paid to S.A. Rm. at Penang by the assessee's Klang firm towards the price and the assessee was debited with this amount on that date. The sale deed was executed on 8th May 1929. In the assessment for the accounting year 13th April 1929 to 12th April 1930 the assessee contended that this sum of Rs. 50,000 must be deemed to have been remitted to him on 3rd April 1929 and not on 8th May 1929 and that it could not therefore be included in the income of the year ending 12th April 1930. On a reference by the Commissioner :

Held, *that the assessee received the money in the shape of house sites only on the 8th May 1929 and so the amount was liable to be assessed to tax in the accounting year ending 12th April 1930.*

Case stated by the Commissioner of Income-tax, Madras, under Section 66 (2) of the Indian Income-tax Act [O. P. No. 3 of 1935].

M. Subbaraya Aiyar and *C. S. Rama Rao Sahib* for petitioner.

M. Patanjali Sastri for the Commissioner of Income tax.

JUDGMENT.

MADHAVAN NAIR, J.—The question referred to us by the Commissioner of Income-tax is: "In what year was the remittance of Rs. 50,000 (Rupees Fifty thousand) received?"

This question arises in connection with an additional assessment imposed upon the petitioner for the year 1930-31 with respect to this amount. The accounting year is the period from 13th April 1929, to 12th April 1930. The question is whether this amount may be considered to have been received by the assessee during this period in the following circumstances.

The assessee is a Nattukottai Chetti doing business in Burma, Klang, Kualalumpur, Penang, etc. On 3rd April 1929, a sum of Rs. 50,000 was debited to his account in his Klang books as having been paid on that date to S. A. Rm. Penang, a money-lending business owned by another Nattukottai Chetti. The entry does not say in what connection this amount was paid. But it is admitted that it relates to the purchase of house sites by the petitioner. He was negotiating for the purchase of certain house sites adjoining his house at Kanadukathan which belonged to S. A. Rm. An agreement to sell land was entered into between the petitioner and S. A. Rm. on 5th April 1929. The sale deed was executed on a later date, on 8th May 1929. The payment of Rs. 50,000 made on 3rd April 1929 was, it may be mentioned, not shown in the accounts of the petitioner as remittance to him in that year. If that was so shown, we may take it that the Income-tax authorities would have assessed him for that amount for the year 1929-1930. On those facts, it was contended by the petitioner that he cannot be taxed under S. 4 (2) of the Income-tax Act for that sum of Rs. 50,000 on the ground that he has received that amount during the accounting period, his case being that he could be considered to have received that amount only on 3rd April, 1929, and not at a later date. Of course, there is no transfer of money in this case, it being understood that the profits were received in the shape of two house-sites. The Income-tax authorities decided that the profits could be said to have been received only on 8th May 1929, when the sale deed was executed and not earlier.

The question for us to determine is whether the money could be said to have been received on 3rd April 1929, or on 8th May

1929. An intermediate position was taken up by the petitioner before the Assistant Commissioner of Income tax who heard the appeal against the order of assessment. It was argued before him that, if the amount was not received on 3rd April 1929, at any rate it should be deemed to have been received on 5th April 1929, when according to him he obtained possession of the property which would be anterior to the date of the sale deed, 8th May 1929. If that argument is accepted, of course it will not be possible to assess him for the amount for the year 1930-1931. But the Assistant Commissioner refused permission to the assessee to raise that point as it was not raised before the Income tax authorities in the first instance. The point is now raised before us and it is pressed that an opportunity should be given to the petitioner to enable him to adduce evidence with a view to establish that he came into possesssion of the house-sites prior to 8th May 1929.

It is evident on a reading of the order passed by the original taxing officer that this question was not raised before him. His agent appeared on behalf of the petitioner and explained the case, and the contentions raised by him are also referred to by the Officer. This question of possession has not been referred to at all in the order. On the other hand, it is said that the assessee actually got possession in the accounting year. The point not having been raised before the taxing officer in the first instance, the appellate authority declined to give permission to the petitioner to raise the point as it was one which could be decided only after hearing the evidence. In the circumstances we think that the refusal by the appellate authority was perfectly justified. We are not inclined to interfere with the discretion of the Income tax authorities in refusing the petitioner to adduce evidence.

So, the only question remaining to be considered is whether it can be said that the money was received by the petitioner on 3rd April 1929, or on 8th May 1929. It is contended that on the date when the money was paid a valuable contractual right had arisen in favour of the petitioner and therefore it must be considered that the money was remitted in law on that date. The argument no doubt is ingenious. But it apears to us that there is no substance in it. The question, strictly speaking, would arise only in a case where the contract to sell stands by itself and

has not been followed by any execution of a sale deed. In this case, first of all, there is the payment, then the contract to sell and then there is the final completion of the whole transaction by the execution of the sale deed. The simple question therefore is, when was the money received in the shape of the house-sites? In the circumstances, there can be only one answer and that is that it was received only on 8th May 1929. That date falling within the year of accounting, the assessee is liable to payment of income tax on that amount.

Various other questions are sought to be raised before us, one of which is that the question arises in connection with the sale of land and not with the remittance of money. That question was not raised at any stage of the case and we are not inclined to hear new points now raised before us.

In the circumstances, we hold that the money was received during the accounting period, 13th April 1929 to 12th April 1930 and that the petitioner is liable to pay income tax on that amount for the year 1930-31. The reference is answered accordingly. The Commissioner will be entitled to get his costs Rs. 250 from the assessee.

Reference answered accordingly.

[In the Lahore High Court.]

TARACHAND POHUMAL

v.

COMMISSIONER OF INCOME TAX, PUNJAB & N. W. F. P.

Sir James Addison and Abdul Rashid, JJ.

February 19, 1936.

Hindu Undivided Family—Registration as firm—Power of Succeeding officer to find that Family is still undivided and to assess as undivided family—Foreign Branches—Remittance to Head Office—Presumption of Remittance from Profits—Effect of Entries in Account Books—Indian Income Tax Act (XI of 1922), Secs. 25-A, 26-A.

The assessees were assessed as a joint Hindu family till 1928-29. In 1929 the then Income-tax officer registered the family as a firm on the basis of a partnership deed without making any enquiry as to whether the members had effected a partition. In the 1933-34 assessment the succeeding officer found that the partnership was confined to the money lending business of the assessees and that the family still continued to be a joint family and assessed the assessees as a Hindu undivided family:

Held, (i) *that a wrong decision of an Income-tax officer in a previous year can be corrected in a subsequent year; (ii) that it was open to the second Income-tax officer to go into the question whether the members of the joint family had in fact separated and that this was a question of fact; (iii) that there was no valid application for registration.*

Held also, *that the ordinary presumption is that money remitted to the headquarters of a firm in British India from a branch situated in a foreign country is profits and not capital unless the assessee proves the contrary; and mere entries in the account books showing that the remittances are made out of capital and that the profits are invested in foreign territory are not sufficient to displace this presumption.*

Cases referred to:—

MURUGAPPA CHETTIAR, *In re* [1926] (I.L.R. 49 M. 465; A.I.R. 1926 M. 767; 97 I.C. 295).

PYARE LAL AND OTHERS v. COMMISSIONER OF INCOME TAX, PUNJAB [1933] (1 I.T.R. 215; A.I.R. 1933 Lah. 827; 7 I.T.C. 31).

RAMLAL MURLIDHAR, *In re* [1931] (I.L.R. 58 C. 1005; 134 I.C. 1056; A.I.R. 1931 Cal. 682; 5 I.T.C. 150).

S. A. SUBBIAH IYER v. COMMISSIONER OF INCOME TAX, MADRAS [1930] (I.L.R. 53 M. 510; A.I.R. 1930 M. 449; 127 I.C. 131).

Case stated by the Commissioner of Income-tax, Punjab and N. W. F. P. under Section 66 (2) of the Indian Income Tax Act (XI of 1922). Civil Ref. No. 75 of 1935.

Kirpa Ram Bajaj, for the assessees.

J. N. Aggarwal, for the Commissioner.

JUDGMENT.

ADDISON, J.—In the matter of the 1933-34 assessment of ncome-tax of Messrs. Tara Chand Pohu Mal of Tarn Taran the ·Commissioner of Income-tax, Punjab, has stated the case and formulated the following questions for the opinion of this Court:—

(1) Whether in the circumstances of this case the petitioners could rightly be assessed under law as a Hindu undivided family?

(2) Has the registration of the firm rightly been refused?

(3) Whether, having regard to the facts of the case inclusion of Rs. 10,000/- is based on any legal data or proper material?

(4) Whether inclusion of Rs. 3,840/- (correctly 3640/-) representing the cess credit brought into British India from Bikaner is justifiable under law in the circumstances of the present case?

The facts of the case are fully stated in the reference. The assessees up till 1928-29 were assessed as a joint Hindu family but during the 1929-30 proceedings a member of the family applied on the 17th May 1929, for the registration of the family as a firm, alleged to have been constituted under an instrument of partnership, dated 4th January 1929. A separate claim was not put into the effect that the Hindu undivided family had disrupted. In that year the Income-tax Officer registered the firm, apparently only on the ground that the document was in proper form. He held no enquiry under Section 25-A (1) as to whether the family had actually effected a partition. The Officer continued to register the firm up to and including the assessment year 1932-33. His successor, who dealt with the 1933-34 assessment found that the status of the assessees was in fact that of a joint Hindu family. The only evidence against this was the partnership deed, already referred to, which was very brief. He held that he was entitled to go behind the deed and find as a fact that it did not represent the real thing.

The deed confined itself to the business of money-lending and agriculture. It did not cover the family's house property, which was very extensive, or shares in other firms. Further, the family's large estate consisting of house and landed property, and

its considerable investments in money-lending and other firms had never been added or classified, much less divided amongst its members. The Income-tax authorities therefore were of opinion that the family could not have separated without some documentary or other evidence on these points. Another circumstance was that though the family is alleged to have disrupted in January 1928, all legal proceedings on its behalf continued to be taken by Chaman Lal on the basis of a power-of-attorney signed by the members of the joint Hindu family as such. The Income-tax authorities further found that the so-called crediting of each member's share of income to his account in the books was fictitious. The profits so credited were those returned for income-tax purposes. These, of course, should be different from the actual profits as some items of expenditure cannot be deducted from the income for tax assessment. Again, the only debits to accounts represented income-tax paid on behalf of each person while the actual expenditure, personal or otherwise, incurred by the four members or their families was indiscriminately charged to a common account. These circumstances (and especially the last) clearly established that this family is still a joint Hindu family and the decision of the Income-tax Officer on the point is supported by ample evidence. It is open to him to go into this question which is an issue of fact (see 5 I.T.C. 150 and 7 I.T.C. 31 etc.). It has long been held that a wrong decision in the previous year by an Income-tax Officer can be corrected in a subsequent year. For the reasons given we answer the first question in the affirmative.

The second question does not therefore arise but we might add that we are in agreement with the opinion of the Commissioner that there was no valid application for registration.

As regards the 5th question the difference between the money received from a shop in Bikaner State and the amount sent there was taken to be profits accruing in British India. This amount was Rs. 3,640/-. The case for the assessees as regards this question is that they are taking the capital out of the shop in Bikaner State into British India and leaving the profit there to be converted into capital in the State. It is clear that the assesseees's books are unreliable in that they are designed to prevent a proper determination of their income and the mere fact that

they show this state of affairs in the Bikaner books is not therefore important. These are said to show that the profits of the Bikaner shop are utilized in purchase and upkeep of house property in the state but that is obviously in the present case merely a fiction in order to show what is taken out of the State as capital in British India. The ordinary presumption is that money remitted to the headquarters of a firm in British India from a branch situated in a foreign country is presumed to be profits and not capital unless the assessee proves the contrary. In the present case he has not done so. (See I.L.R. 49 Mad. 465 and I.L.R. 53 Mad. 510). We therefore answer the fifth question in the affirmative.

The third and fourth questions relate to the same matter. The Income-tax Officer found an omission of Rs. 200/- in the return as regards interest. It is alleged that this was due to an oversight. There were other omissions as well and as the total value of these could not be accurately determined he added a sum of Rs. 10,000/- to the income shown in the books. The finding in fact was that the account did not represent a complete and correct version of the actual business. The account books are kept in a special script for the deciphering of which the assessee's word has to be accepted. Interest items were not shown in the cash books; nor was an interest account maintained, though a list was prepared at the end of the year from the personal accounts of the debtors. For these reasons the Income-tax Officer held that the books did not give a complete and correct version of the actual business and though he accepted them to a certain extent, he added a sum of Rs. 10,000/- to represent the amount of omissions. In making an assessment it is correct that the Income tax Officer shall proceed on judicial principles but in the present case there was evidence before him to show that the books could not be relied upon. We are therefore of opinion that the third and fourth questions should also be answered in the affirmative.

The Commissioner will get his costs.

Reference answered accordingly.

[IN THE LAHORE HIGH COURT.]

Diwan Bahadur SIR T. VIJAYARAGHAVACHARYA

v.

COMMISSIONER OF INCOME TAX, PUNJAB, N.W.F.P. AND DELHI.

SIR JAMES ADDISON AND ABDUL RASHID, JJ.

February 25, 1936.

PENSION—CIVIL SERVANT RESIDING IN INDIA—PENSION RECEIVED IN ENGLAND—WHETHER ASSESSABLE—'ACCRUE,' 'ARISE,' MEANINGS OF—PLACE WHERE PENSION ACCRUES—RULE EXEMPTING PENSIONS PAID TO NON-RESIDENTS WHETHER SUPERFLUOUS—INDIAN INCOME TAX ACT (XI OF 1922), SECTIONS 4 (1), 60, 18 (2), 7 (2).

The words 'accruing or arising' involve the concept of receivability or the right to receive in a particular place and do not refer to income being earned in that place or being derived from a source of income situated in that place, and consequently income accrues or arises in the country where there is a right to demand payment of it or where in fact it is paid and not necessarily in the country where it is earned or where the source of the income is situated.

The assessee retired from the Madras Civil Service and was granted a super-annuation pension of Rs. 9,500. Under Article 933 of the Civil Service Regulations when a pension is stated in rupees it is payable at any treasury in India or at the pensioner's option at the Home Treasury. The assessee though a resident in British India drew the pension in London and the money was not brought to British India. The question being whether this income accrued or arose to the assessee in British India within Sec. 4 of the Indian Income Tax Act and could be assessed to income-tax in British India : Held, *that, as the assessee had a right to receive the pension in London and received it in London, it did not accrue or arise in British India, within the meaning of Section 4 of the Indian Income Tax Act and was not assessable to income-tax in British India.*

Pension is different from pay. It is a right to receive a certain sum of money annually in a particular place.

The notification issued under Sec. 60 of the Indian Income Tax Act, exempting pay, leave salaries and pensions paid outside India in the case of persons residing out of India is superfluous as pensions etc. drawn as of right in the United Kingdom do not accrue in British India.

Cases referred to :

BOARD OF REVENUE, MADRAS *v.* ARUNACHALAM CHETTIAR, [1921] (I.L.R. 44 Mad. 65 ; 59 I.C. 482 ; A.I.R. 1921 Mad. 427 ; 1 I.T.C. 75).

COMMISSIONER INCOME TAX, BOMBAY *v.* BANSILAL MOTILAL [1930] (I. L. R. 54 Bom. 460 ; A. I. R. 1930 Bom. 381 ; 125 I.C. 691).

COMMISSIONER OF INCOME TAX, BURMA *v.* PHRA PHRAISON SALARAK [1929] (I.L.R. 6 Rang. 598 ; A.I.R. 1929 Rang. 1 ; 114 I.C. 296).

ROGERS PRATT SHELLAC & CO. *v.* SECRETARY OF STATE [1925] (I.L.R. 52 Cal. 1 ; 83 I.C. 273 ; 1 I.T.C. 363 ; A.I.R. 1925 Cal. 34 ; 28 C.W.N. 1074).

SAUNDERS, *In re* [1931] (I.L.R. 54 All. 223 ; A.I.R. 1932 All. 151 ; 137 I.C. 84 ; 5 I.T.C. 454).

Case stated by the Commissioner of Income tax, Punjab and N.W.F.P., and Delhi under Sec. 66 (2) of the Indian Income Tax Act in the matter of the assessment of Sir T. Vijayaraghavacharya for the year 1933-1934.

The facts are stated in the judgment.

Mehr Chand Mahajan for the assessee.

J. N. Aggarwal, S. M. Sikri, and *M. Aslam Khan* for the Commissioner of Income Tax.

JUDGMENT.

Under Section 66 (2) of the Indian Income Tax Act, the Commissioner of Income Tax, Punjab, has stated the case of Diwan Bahadur Sir T. Vijayaraghavacharya, K. B. E., for

the assessment year 1933-34 and had referred for the opinion of this court the following question of law :—

"The assessee having received in the United Kingdom payments of pension granted by the Madras Government under the Civil Service Regulations of the Government of India (as further described in the case), were such payments in so far as they were not brought into British India with the effect of attracting subsection (2) of section (4) of the Indian Income Tax Act, income accruing or arising in British India within the meaning of section 4 (1) of the Act?"

The facts have been very fully stated by the Commissioner and need only be briefly referred to. The assessee was appointed to the Madras Provincial Civil Service in 1898 and served there except for certain periods when he was employed under the Central Government on deputation outside India and for a period when he was a member of the Public Service Commission. Since the 15th September 1929 he has been Vice Chairman of the Imperial Council of Agricultural Research and continues to hold that post though he retired from the Madras Civil Service on the 27th of August 1930 when he was granted superannuation pension of Rs. 9,500. Article 933 of the Civil Service Regulation is to the effect that when a pension is stated in rupees, it is payable at any Treasury in India, or, at the pensioner's option, at the Home Treasury. The assessee for the year in question was a resident in British India but he drew the pension in London. The Income Tax authorities have held that he was liable to pay income tax on £743 with respect to that pension in addition to other income. This amount of £743 converted back into rupees at the current rate of exchange comes to Rs. 9,907, and this is the sum in contention.

Section 4 of the Act runs as follows :—

" 4 (1) Save as hereinafter provided, this Act shall apply to all income, profits or gains, as described or comprised in section 6, from whatever source derived, accruing or arising, or received in British India, or deemed under the provisions of this Act to accrue or arise, or to be received in British India.

(2) Income, profits and gains accruing or arising without British India to a person resident in British India, shall, if they are received in or brought into British India, be deemed to have

accrued or arisen in British India and to be income, profits and gains of the year in which they are so received or brought, notwithstanding the fact that they did not so accrue or arise in that year.

In the present case it is admitted that the money was not brought into British India. The assessee's contention was that the income did not accrue or arise in India nor was it received in India and that he had a vested right to draw it in London.

Under Section 60 of the Act a notification has been issued exempting pay, leave salaries, and pensions paid outside India in the case of persons residing out of India, so that this exemption does not help the assessee, but it was contended before us that this exemption is a superfluity, as the word " accrues " cannot be held to apply to pensions drawn as of right in the United Kingdom. The subject is discussed at length at pages 327 *et seq* of *Sundaram's Law of Income Tax in India* and his view is that the exemption in question is superfluous. The difficulty arises from the meaning to be attached to the words " accruing " or " arising." Do they mean receivability in a particular place or do they involve the concept of the income either being earned in that place or being derived from a source of income situated in that place ? Now the words " from whatever source derived " in section 4 (1) have no meaning if they refer only to the sources described in section 6 and the natural meaning to be given to them would be to construe them as referring to sources both within and outside British India. If that is so, the word " accrue " cannot mean earned or derived from a source in British India and the meaning to be attached to it would be that of receivability or rather perhaps the right to receive it in a particular place. Section 4 (2) of the Act suggests that " accruing " refers more to the receiving or right to receive than to the place of origin.

In this connection section 18 (2A) may be referred to. It runs as follows :—

" Notwithstanding anything hereinbefore contained, for the purpose of making the deduction under sub-section (2), there shall be included in the amount payable any income chargeable under the head " Salaries " which is payable to the assessee out

of India by or on behalf of Government, and the value in rupees of such income shall be calculated at the prescribed rate of exchange ".

By this sub-section salaries payable to Government servants out of India by or on behalf of Government are taxable, but this does not necessarily mean that they accrue or arise in British India. Section 4 (1) starts with the saving words " save as hereinafter provided ", and Section 18 (2 A) may, therefore, be treated as an exception to Section 4 (1). Again, as already mentioned, leave salaries and pensions paid out of India have been exempted under Section 60 of the Act and the argument therefore is that they are taxable, *i.e.*, that they have accrued in British India. If this is so. accruing would mean earned. See again Section 7 (2) of the Act which runs as follows :—

" Any income which would be chargeable under this head (of salaries) if paid in British India shall be deemed to be so chargeable if paid to a British subject or any servant of His Majesty in any part of India by Government or by a local authority established by the Governor-General in Council ".

It must be argued from this sub-section that salary paid to an Indian Government servant in India but outside British India does not accrue in British India. This shows the confusion with respect to this question. Under Section 7 (2) the salary of a political officer in a Native State is taxable, but an Indian Government servant, who draws his pay or leave-salary in England, is protected by the notification under Section 60. It would follow that either Section 7 (2) or the exemption about pay of officers on deputation in the United Kingdom or a Colony is superfluous. In our opinion it is the notification that is superfluous as it is difficult to hold that pay accrues in British India if it is paid outside.

Further, pension is different from pay. It is a right to receive a certain sum of money annually at a particular place.

In the present case it can be paid in India or in London. The pensioner has the right to receive it in London and he receives it there. The subject was touched upon in *Commissioner of Income Tax, Burma* v. *Phra Phraison Salarak* (*6 Rang. 598*). ORMISTON, J., at the bottom of page 601 of the report said : " In Murray's Oxford Dictionary the words ' accrue ' and ' arise ' are

regarded as synonymous. In the Century Dictionary the word 'accrue' is defined to mean 'to become a present or enforceable right to demand'. Stroud defines 'arising in the United Kingdom' as 'coming into the person's hands in the United Kingdom.'

In *Rogers Pratt Shellac & Co.* v. *Secretary of State* (I.L.R. 52 Cal. 1 at page 30), MUKERJI, J., after discussing the theoretical distinction between "accruing" and "arising" arrives at the conclusion that the words denote the same idea or ideas very similar, and that both words are used in contradiction to the word "receive" and indicated a right to receive. They represent, he says, a stage anterior to the point of time, when the income becomes receivable and connote a character of income which is more or less inchoate. These definitions do not support the view that "income accrues or arises in a particular country" by reason of the fact that it is earned in that country and on the contrary go to show that income accrues or arises in the country where there is a right to demand payment of it or where in fact it is paid.

With great respect we are in agreement with the argument set forth by ORMISTON and MUKERJI, JJ., and if it is accepted, it is decisive of the present case.

Another decision which may be referred to is *Board of Revenue, Madras* v. *Arunachalam Chettiar* (I.L.R. 44 Mad. 65). At page 75 it is brought out that the Board of Revenue in Madras interpreted the words accruing and arising as meaning "becoming the subject of a right to receive". Again at the bottom of page 78 it was said: "The words 'accrue' and 'arise' are no doubt usually confined to moneys which are due but not received and hence are used as alternatives to 'received'".

There is a decision of the Allahabad High Court, *Saunders, In re* (54 All. 223), where a certain allowance was held to come within the term "salary" and, though payable in London, was held to accrue or arise in British India. It was sought to argue from this decision that the word "accruing" means "earned" and that the assessee's pension was earned in India. With great respect it seems to us that this is to go too far.

Reliance is also placed on behalf of the Commissioner on *Commissioner of Income-tax* v. *Bansilal Motilal* (I. L. R. 54

Bom. 463) where the words "accruing" or "arising" were held to be different from the expression "received" and indicated some origin or source of growth for the income in question. It may be admitted that this decision is more in favour of the Commissioner than of the assessee.

On the whole we are of opinion that the question referred should be answered in the negative and we also hold that the assessee should have his costs here.

Reference answered in the negative.

[IN THE PRIVY COUNCIL.]

THE COMMISSIONER OF INCOME TAX, BOMBAY PRESIDENCY AND ADEN

v.

THE BOMBAY TRUST CORPORATION, LTD.

LORD ATKIN, LORD THANKERTON, SIR SHADI LAL, SIR GEORGE RANKIN AND SIR GEORGE RICH.

July 17, 1936.

NON-RESIDENTS—FOREIGN COMPANY LENDING MONEY TO INDIAN COMPANY—ASSESSMENT OF INDIAN COMPANY AS AGENT OF FOREIGN COMPANY ON INTEREST PAID TO LATTER—LEGALITY—MONEY LENT BY AND INTEREST PAID TO COMMON BANKER—LIABILITY OF FOREGIN COMPANY TO ASSESSMENT—VALUE OF ENTRIES IN ACCOUNTS—NECESSITY OF EVIDFNCE TO SHOW INCOME ACCRUED TO FOREIGN COMPANY—REFERENCE—ORDER OF HIGH COURT—POWER OF COMMISSIONER TO ORDER FURTHER INQUIRY—DEMANDING SECURITY AS CONDITION FOR REFUND—LEGALITY—MANDAMUS—POWER OF HIGH COURT TO ISSUE MANDAMUS IN INCOME TAX MATTERS—INDIAN INCOME TAX ACT (XI OF 1922), Secs. 42 (1), 43, 33 (2), 66—SPECIFIC RELIEF ACT (II OF 1877), Sec. 45 (g).

Until November 1926 a company, hereinafter referred to as the Bombay Company, borrowed money in large sums from the Hong Kong Company at interest upon fixed deposit and the Bombay Company was assessed to income tax under Sec. 43 of the

Indian Income Tax Act as agent of the Hong Kong Company in respect of the interest paid by it to the Hong Kong Company. In November 1926, all the fixed deposits were converted to call loan and paid to the Hong Kong Co. through a common banker, namely, E. D. Sassoon Co., Ltd., Shanghai Branch. In the year 1927 entries were made in the accounts of the companies upon the footing that there was no longer any loan from the Hong Kong Company. The Bombay Company borrowed a loan of 6½ crores in taels from E. D. Sassoon Ltd., Shanghai Branch, and paid interest thereon to this Company. The income tax authorities sought to assess the Bombay Company on the interest so paid in 1927 also as being in effect interest paid to the Hong Kong Company as all the companies were closely associated concerns and worked in concert:

Held, *that it was necessary for such assessment that there should be some evidence to show that in 1927, the loan from the Hong Kong company continued and that interest 'accrued or arose' to that company thereon. As the entries in the books showed no payment to the foreign company and nothing was due to it, the Income-tax Authorities could not without evidence insist upon a right to treat entries showing a* tael *loan of six and a half crores made by another Company, and interest calculated in* taels *paid thereon as evidence that a somewhat similar amount was due from and was being paid by the Bombay Company to the Hong Kong company. Such evidence was lacking and there was nothing to entitle the Income tax Authorities to hold that in 1927, the Hong Kong Company was in receipt of profits and gains from the Bombay Company, and to assess the latter as an agent.*

It is very necessary that orders made under the Specific Relief Act should specify with exactitude and clarity the specific act which the person holding a public office is being commanded to do.

Where, after the High Court had given judgment that there was no evidence on which the Income tax Authorities could in law find that a foreign company was receiving from a company in India any sums as interest on money lent, the Income Tax Commissioner directed the Assistant Commissioner to take back the

appeal on his file, to set aside the assessment and to direct the Income Tax Officer to make a fresh assessment after making such further enquiry as he might think fit and directed refund of the tax on condition that the assessee gave security for payment of the amount in case a fresh assessment was made or an appeal to the Privy Council was successful :

Held, *that it could not be said that by the High Court's judgment, the Commissioner was obliged to discontinue proceedings against the Bombay Company as agent of the foreign company in respect of the year of assessment. It was within the jurisdiction of the Commissioner to direct further enquiry if he thought such enquiry to be reasonable and to be profitable in the public interest. Under S. 33 (2) he has a general power to make enquiry or to cause an enquiry to be made, although as the whole question at issue was whether or not the foreign company, or the Indian Company as its agent, were liable to be assessed at all, to direct the Income Tax Officer to make a fresh assessment after making such further enquiry as he thought fit was an inappropriate form of order. But the Commissioner acted illegally in demanding security as a condition for refunding the tax.*

Clause (g) in S. 45 of the Specific Relief Act, does not mean that orders can be made to enforce the satisfaction of a claim upon the Crown provided that the Court acts with some additional motive or has some further intention, e.g., *for enforcing the orders made by the High Court. The principle is that the Court cannot claim even in appearance to command the Crown, and where an obligation is cast upon the principal the Court cannot enforce it against the servant merely as such and before mandamus can issue to a public servant it must, therefore, be shown that a duty towards the applicant has been imposed upon the public servant by statute so that he can be charged thereon, and independently of any duty which as servant he may owe to the Crown, his principal.*

Quaere.—*Whether the Commissioner of Income tax, either generally or under S. 66, Sub-S. 5 of the Income Tax Act, is in this position as regard the refund of tax paid under an invalid*

The decision of the High Court upon a question referred to it under Sec. 66 of the Income Tax Act is advisory.

Cases referred to:—

ALCOCK ASHDOWN & CO v. CHIEF REVENUE AUTHORITY, BOMBAY [1923] (50 I.A. 227; 47 Bom. 742; 25 Bom. L.R. 920; 75 I.C. 392; A.I.R. 1923 P.C. 138; 1 I.T.C. 221).

BARON DE BODE'S CASE [1838] (6 Dowl. 776).

COMMISSIONER OF INCOME TAX, BOMBAY v. BOMBAY TRUST CORPORATION LTD. [1930] (I.L.R. 54 Bom. 216; 57 I.A. 49; 121 I.C. 532; A.I.R. 1930 P.C. 54; 4 I.T.C. 302).

COMMISSIONERS FOR SPECIAL PURPOSES OF INCOME TAX v. PEMSEL [1891] (1891 A.C. 531; 61 L.J.Q.B. 265; 65 L.T. 21; 3 Tax Cas. 53).

REGINA v. LORDS COMMISSIONERS OF THE TREASURY [1872] (7 Q.B. 387; 41 L.J.Q.B. 178; 26 L.T. 64).

TATA IRON & STEEL CO. v. CHIEF REVENUE AUTHORITY [1923] (50 I.A. 212; 47 Bom. 724; 4 I.C. 469).

A. M. Dunne, K. C. and *Sir Thomas Strangman*, for the Appellants.

Raymond W. Needham and *Reginald P. Hills*, for the Respondents.

SIR GEORGE RANKIN.—In this case two appeals from the High Court at Bombay have been consolidated. Both appeals are brought by Income tax Authorities and both arise out of proceedings to assess a company registered outside British India called the Hong Kong Trust Corporation, Limited (herein referred to as the Hong Kong Company) to income tax in respect of the year of assessment 1928-29. The Income tax Authorities have claimed to be entitled to assess the Hong Kong Company in the name of the Bombay Trust Corporation, Limited (herein called the Bombay Company) as its agent under the provisions of Section 42 (1) and Section 43 of the Indian Income Tax Act, 1922, that is, upon the footing that in the year 1927 profits and gains accrued or arose to the Hong Kong Company through its business connection with the Bombay Company. The Income-

tax Officer having on March 29, 1930, made an assessment upon this footing the matter came on appeal from him before the Assistant Commissioner. The Assistant Commissioner, on July 12, 1930, confirmed the assessment. The Bombay Company having requested the Commissioner to make a reference to the High Court under Sec. 66 of the Act, the Commissioner, on March 2, 1931, exercised his powers of review under Sec. 33, and remanded the appeal for a fresh decision by the Assistant Commissioner after taking certain further evidence. In the end the Assistant Commissioner on October 9, 1931, assessed the Bombay Company as agent of the Hong Kong Company upon a sum of Rs. 20,50,000 which involved a liability to tax, including super-tax of Rs. 3,17,187-8-0. On December 8, 1931, the Bombay Company again applied to the Commissioner for a reference of certain questions of law to the High Court. This the Commissioner refused to do, but upon application made to the High Court for an order under Sec. 66, sub-sec. 3, the High Court by order dated October 6, 1932, required the Commissioner to refer the following question of law:

"Whether there was any evidence to justify the finding of the Assistant Commissioner that for the year of assessment, profits and gains accrued or arose to the Hong Kong Trust Corporation through its business connection with the Bombay Trust Corporation."

The Bombay Company had in the meantime, on April 6, 1932 paid under protest Rs. 3,17,187-8-0 the amount of the tax assessed. The Commissioner having stated a case for the opinion of the High Court upon the question propounded, and having further stated his opinion that the question should be answered in the affirmative, the High Court on August 29, 1933, gave judgment answering the question in the negative, and directing the costs of the reference to be paid to the Bombay Company. It is from this decision that appeal No. 1 of 1930 has been brought, and their Lordships will first deal with this appeal.

The main evidence upon the question whether in the year 1927 sums of money were paid by the Bombay Company to the Hong Kong Company by way of interest upon money lent con-

sists of entries in the books of the Bombay Company. Exhibited to the case stated by the Commissioner are extracts from the ledger of the Bombay Company taken from the accounts of the Hong Kong Trust Corporation, Limited, "Fixed Deposit Account', and "Call Loan Account" and of E. D. Sassoon and Company, Limited, "Shanghai Loan Account" and "Shanghai Current Account." These books show clearly enough that until November of the year 1926 the Bombay Company was borrowing money in large sums from the Hong Kong Company at $5\frac{1}{2}$ per cent. interest upon fixed deposits, that is, in every case or almost every case, upon deposit for one year certain. In 1924, 1925 and for almost the whole of 1926 different sums are shown as being lent for one year upon different dates, and interest thereon is shown as remitted to the Hong Kong Company by debits to the account of the Bombay Company in the books of E. D. Sassoon and Company, Limited, at Shanghai, who were bankers to both parties.

It is not open to dispute that in October, 1926, the Income tax Authorities served a notice upon the Bombay Company to show cause why it should not be treated as an agent of the Hong Kong Company under Sec. 43. From documents which are in evidence it is further clear that on October 27, 1926, the Bombay Company telegraphed to the Hong Kong Company to enquire whether they were agreeable to all their deposits with the Bombay Company being on call as from the dates of the deposits. On October 28, a reply was received from the Hong Kong Company agreeing to this proposal. On November 13, the Hong Kong Company telegraphed requiring repayment of their deposits amounting to Rs. 11,01,85,918 through Messrs. E. D. Sassoon and Company, Limited, of Shanghai. On November 16 and 17 the Income tax Officer came to a finding that the Bombay Company should be held to be agent of the Hong Kong Company, and called for a return upon that footing. On November 19, the Bombay Company wrote to Messrs. E. D. Sassoon and Company, Limited, of Bombay asking them to remit to Messrs. E. D. Sassoon and Company, Limited, Shanghai (whom their Lordships will refer to as the Shanghai branch), the sum of Rs. 11,42,29,931-10-9. They also wrote to the Shanghai branch advising that they had remitted this amount through

Messrs. E. D. Sassoon and Company, Limited, Bombay, the amount being made up as follows :—

	RS.	AS.	P.
Amount of Call Loans repaid by you on our behalf ...	11,04,85,918	0	10
Interest on above ending November 16, 1926 ...	37,44,013	9	11
	11,42,29,931	10	9

On the same day also the Bombay Company wrote to the Hong Kong Company saying that they had advised Messrs. E. D. Sassoon & Company, Limited, Shanghai, to credit their account with these sums.

In complete accordance with this correspondence entries are made by the Bombay Company in their ledger. Thus an account called the "Hong Kong Trust Corporation, Limited, Call Loan Account" is opened with a credit entry of November 13, 1926, showing sums amounting for interest and principal to the figure already mentioned on the footing that the principal loans were taken originally as fixed deposits for one year and are now converted into call loans. On the debit side of this account there is an entry dated November 17, "to E. D. Sassoon and Company, Limited, for amount being repayment of loans with interest ending November 16, 1936." The E. D. Sassoon and Company, Limited, Shanghai, Loan Account" shows at the same time a credit to the Shanghai branch " for amounts borrowed by E. D. S. & Co., Shanghai, on our account being equivalent of Taels 6,50,00,000, at Exchange 170 bearing interest at 5¼ per cent. per annum" together with a credit of interest to the end of the year upon this loan. Within a short time, namely, on December 6, 1926, an entry states that three out of the six and a half crores of taels borrowed were repaid to the Shanghai branch. Throughout 1927 entries are made upon the footing that there are no longer any sums received on loan from the Hong Kong Company in respect of fixed deposits, call loans or otherwise, but that the Bombay Company has received from the Shanghai branch a loan in taels on which interest at 5¼ per cent. is being paid. When the present matter was first before

the Assistant Commissioner he requested the Bombay Company to obtain a declaration from the Hong Kong Company and from Messrs. E. D. Sassoon & Company, Limited, Shanghai, on certain specific questions which he formulated. These declarations were duly made, the Chief Accountant of the Shanghai branch declaring that his company made a payment on November 17, 1926, to the Hong Kong Company of the eleven crores of rupees and that the Shanghai branch made a tael loan of six and a half crores to the Bombay Company but did not borrow any portion of that loan from the Hong Kong Company, and that the Shanghai branch had not since November 17, 1926, borrowed any taels from the Hong Kong Company or paid to that Company any interest which they themselves had received from India. There was a further declaration from Mr. Priestly, Director of the Hong Kong Company stating that the Bombay Company on November 17, 1926, paid off the loans and that the Hong Kong Company had made no new loan of six and a half crores of taels to the Bombay Company or to Messrs. E. D. Sasson & Company, Limited, and that there were no transactions between the Bombay Company and the Hong Kong Company in 1927. This declaration was accompanied by the certificate of a firm of chartered accountants, auditors to the Hong Kong Company. At a later stage, namely, in June, 1931, a letter from Sir Victor Sassoon was put into the effect that in 1926 when he was in China he set to work to make arrangements on behalf of the Bombay Company so that after his return to India that company was in a position to send the telegram of October 27, 1926.

When the Commissioner, in compliance with the High Court's order came to state in his letter of reference the evidence which existed in support of the conclusion that in 1927 the Hong Kong Company had been in receipt of interest from the Bombay Company he set forth the correspondence already referred to as taking place in October and November, 1926, and the facts as to the notifications made by the Income-tax Officer in October and November showing that he proposed to charge the Bombay Company with tax as agents for the Hong Kong Company. He set forth also that the amount of the original loan was very large, over eleven crores of rupees, and that the Hong Kong Company, the Bombay Company and the Sassoon

Company at Bombay and Shanghai were all closely associated concerns, their share capitals being held almost exclusively by members of the same family. Also that the Hong Kong Company was "practically formed to finance the Bombay Company", the former having a paid up capital of 8 crores and the latter of 1 crore; while both had large resources in addition thereto from their banking or financing businesses.

Their Lordships are well satisfied that all these companies were closely associated, that in the words of Secs. 42 and 43 there was a business connection between them and that they were working in this matter in concert as though under one control. Indeed it is now clear that so long as the Hong Kong Company was lending money at interest to the Bombay Company, the former company was in receipt of profits or gains taxable under Secs. 42 (1) and 43. This matter was thrashed out by litigation in respect of the transactions which took place in 1924-25 and the liability under these sections was confirmed by a judgment of this Board in *Commissioner of Income-tax, Bombay Presidency* v. *Bombay Trust Corporation, Limited.* Tax was paid without contest in respect of the transactions of 1926. The question is whether there was any evidence upon which the Income-tax authorities could in law find that in 1927 the Hong Kong Company was receiving from the Bombay Company any sums as interest on money lent.

In their Lordships' opinion the High Court at Bombay have rightly answered in the negative the question referred to them. However sceptical the attitude which the Income tax authorities may think fit to adopt towards the declarations offered and the entries made in the Bombay Company's books, it is necessary, if the assessment made is to be supported, that there shall be some evidence to show that in 1927 the loan from the Hong Kong Company continued and that interest "accrued or arose" to that company thereon. If the entries in the books show no payment to the Hong Kong Company, and nothing due to the Hong Kong Company, the Income tax authorities cannot without evidence insist upon a right to treat entries showing a tael loan of six and a half crores made by a Shanghai Company, and interest calculated in taels paid thereon, as evidence that a somewhat similar amount was due

from and was being paid by the Bombay Company to the Hong-Kong Company. The only rule of evidence to be discovered in the Indian Evidence Act having any bearing upon this question would appear to be illustration (*d*) to Sec. 114 of the Indian Evidence Act:—

"The Court may presume that a thing or state of things which has been shown to be in existence within a period shorter than that within which such things or state of things usually cease to exist is still in existence".

This rule cannot in the present case supply the want of evidence. Their Lordships are not considering a case in which by reason of the entries in an assessee's books of account being inconsistent, or by reason of positive evidence showing that certain entries in his books are erroneous or fraudulent, the value of the books as evidence can be considered as overthrown. On the contrary, though the Income tax authorities have been somewhat slow to appreciate it, the circumstance that in October or November, 1926, it was disclosed that the transactions between the Hong Kong and Bombay companies were to be charged with Indian income tax means that the persons interested and in control of these closely associated companies had the strongest reasons for desiring to change their course of business (not merely for pretending to change it) so as not in the future to attract the tax. The Hong Kong Company from a taxpayer's point of view had two plain disqualifications as a lender; it had a business connection in India and it had a large capital of its own upon which it did not need to pay interest. It is altogether credible, therefore, that the persons in ultimate control of all the associated companies, should desire to pay off the Hong Kong Company and to obtain another financier for the Bombay Company. By entries regularly made in its books, and by other evidence the Bombay Company says that this is what it did. What is the evidence to the contrary—evidence, that is to say to show that throughout 1927 payments were being made to the Hong Kong Campany, that what purported to be the making of a tael loan was a fiction, and that entries of payments of interest upon a tael loan were in reality reference to payments of interest to the Hong Kong Company?

Their Lordships agree with the Bombay High Court in thinking that such evidence is altogether lacking. The Income tax authorities in arriving at the contrary opinion have insufficiently considered that the question at issue has to be decided according to the legal rights resulting to the parties from what they in fact did and agreed to. If the Hong Kong Company really accepted a credit in the books of the Sassoon Company at Shanghai in discharge of their loans to the Bombay Company, and if the latter really intended to become liable to Sassoons at Shanghai for a debt in taels then the Bombay Company succeeded in changing its financier. The only evidence in the case is evidence to that effect, and a mere refusal to believe in the evidence to that effect is not, in the absence of any positive evidence, sufficient to entitle the Income-tax authorities to hold that in 1927 the Hong Kong Company was in receipt of profits and gains from the Bombay Company.

Comment has been made by different income-tax officials that the Bombay Company has not produced the books of the Hong Kong Trust Corporation which are at Hong Kong. Also and less unreasonably, that the Bombay Company was at first unwilling to disclose the name of the firm from which the Sassoon Company at Shanghai obtained the finance which enabled them to make the tael loan to the Bombay Company. At a later stage of the proceedings, the Bombay Company, the assessees, stated that Sassoons of Shanghai obtained this finance from a company called Arnold and Company in China. It is said also that Arnold and Company is closely associated with the Sassoon Companies. If on these lines it could be shown—not that Arnold and Company lent the money and became entitled as upon a tael transaction with Sassoons of Shanghai to the rights of a lender—but that the tael loan made by Sassoons was in fact and in law made by the Hong Kong Company, no doubt there would be something upon which the assessment order could be supported. But the case stated discloses no evidence to show the falsity of any of the entries in the books or the unreality of the correspondence of October and November, 1926, supported as these are by the declarations for which the Assistant Commissioner had asked. The comments above noted do not supply the place of such evidence. The Bombay Company made the

repayment in the same manner as it had received payment, namely, by the agency of the common banker. On no view is it possible to suppose that the transactions of 1927 were the same in character as the transactions of the previous years. If it is to be held that very different transactions are in substance the same in character, the basis of such a finding must be evidence. The appeal from the judgment of the High Court dated August 29, 1933, fails.

It remains to consider the events that followed upon the decision of the High Court. By the terms of Sec. 66 applicable to the present case, upon receipt of a copy of the judgment it became the duty of the Commissioner to "dispose of the case accordingly." The assessee company contended that the High Court's decision was final in the sense that it put an end to any right on the part of the Income-tax authorities to continue the proceedings to assess them as agent for the Hong Kong Company for that year of assessment, namely, 1928-29. On this view the duty of the Commissioner would be to set aside the assessment order, to refund the tax which had been paid and to discontinue all further proceedings. The Commissioner took another view. He does not seem to have been furnished with a copy of the High Court's judgment until October 14, 1930. On January 16, 1934, he directed the Assistant Commissioner to take back the appeal on his file, to set aside the assessment and to direct the Income-tax Officer to make a fresh assessment after making such further enquiry as he might think fit. He also directed that the tax paid should be refunded with interest provided that Messrs. E. D. Sassoon & Company, Limited, undertook to be responsible for paying back the amount in case an assessment was levied again or the matter was taken on appeal to the Privy Council. On January 30, 1934, the Income tax Officer acting under Sec. 22 of the Act required the Bombay Company as agent of the Hong Kong Company to produce or cause to be produced on February 15, 1934, the books of account of the Hong Kong Company for the year ended December 31, 1927. He also required the Bombay Company as such agent to produce at the same time any evidence on which it might rely in support of its original return. On February 5, the Solicitors for the assessees wrote to the Commissioner claiming that this procedure

was unwarranted and asking whether it was proposed to proceed upon the notices issued by the Income-tax Officer pending application for leave to appeal to the Privy Council. On February 15, the assessees appeared under protest before the Income-tax Officer. On February 20, the Income-tax Officer purported to make an assessment under sub-Sec. 4 of Sec. 23 of the Act because of the failure of the Bombay Company to produce the books of the Hong Kong Company upon that date. He invited the assessees, however, to make an application under Sec. 27 to set aside this assessment. At the same time he purported to act under Sec. 48 (A) of the Act and to set off the amount due upon this fresh assessment against the refund due to the assessees under the order of January 16, 1934. The application under Sec. 27 having been made (together with an appeal preferred before the Assistant Commissioner notwithstanding the proviso to sub-Sec. (1) of Sec. 30) the assessees were informed on July 5, 1934, that proceedings in respect of the appeal were postponed until the hearing of the appeal by the Commissioner to His Majesty in Council against the decision of the High Court on the reference. The application under Sec. 27 was likewise kept in abeyance until the decision of the appeal now before the Board. Thereupon on August 23, 1934, the Bombay Company applied by motion to the High Court of Bombay under Sec. 45 of the Specific Relief Act, 1877, for an order in the following terms:—

"(*a*) That the Commissioner of Income-tax, Bombay Presidency, be ordered to refund and pay back to the petitioners the sum of Rs. 3,17,187-8-0, being the assessment levied on the Petitioners and being the subject-matter of Civil Reference No. 8 of 1933 under the Indian Income Tax Act referred to in the affidavit of Mr. A. E. J. Brander and disposed of by this Honourable Court in its appellate side by judgment delivered on the 29th day of August 1933, with interest on the said sum."

"(*b*) That the Assistant Commissioner of Income-tax, Bombay, may be ordered to proceed with and dispose of the appeal filed by the Petitioners on the 14th day of March 1934, against the summary assessment levied by the Income-tax Officer, Companies Circle, Bombay, by his notices dated the 20th day of February 1934, referred to in the affidavit aforesaid."

"(c) That the Income-tax Officer, Companies Circle, Bombay, be ordered to proceed with and dispose of the application made by the Petitioners under Sec. 27 of the Income tax Act on the 14th day of March 1934 against the summary assessment levied by the Income-tax Officer by his notices of assessment dated the 20th day of February 1934, and referred to in the affidavit aforesaid."

This application was dealt with by the High Court, Beaumont, C. J. and Rangnekar J., on September 19, 1934. The High Court made an order whereby the Commissioner was directed to set aside the original assessment and to repay to the petitioners the sum of Rs. 3,17,187-8-0 with certain interest and costs. The learned Judges made no order under paras. (b) and (c) of the notice of motion saying that they thought they were unnecessary. It is from this order that appeal No. 89 of 1935 has been brought.

From the judgment of the learned Chief Justice it appears that the Court considered that, as a result of the previous order of the High Court, the proceedings should have been terminated forthwith. They were of opinion that the Commissioner had no jurisdiction to direct the Assistant Commissioner to take back the appeal to him. They also considered that there was no justification for directing the Income-tax Officer to make further enquiry, because the whole assessment was covered by the judgment of the Court, and the Income-tax Officer had already obtained production of all the documents for which he asked. The learned Chief Justice commented with some severity upon that part of the order of the Commissioner which imposed as a condition of refund that a guarantee should be given by E. D. Sassoon and Company, saying that the Commissioner must have known perfectly well that he was not justified in imposing as a condition of the refund that a guarantee should be given by some third party for the amount of any fresh assessment. He further observed with reference to the order under Sec. 23 (4) made by the Income-tax Officer on February 20, 1934, that it was perfectly obvious, and the Income-tax Officer must have known, that it would not be possible for the assessees to produce within fifteen days books of account of the Corporation in Hong Kong, a corporation which according to the finding of the Court had no

business connection with the assessees. He described the procedure adopted by the Income-tax authorities as a flagrant attempt to flout the judgment of the Court and to assess the assessees in a large sum in respect of which the court had held that there is no evidence to justify the assessment. It being objected that by cl. (g) of Sec. 45 of the Specific Relief Act nothing in that section "shall be deemed to authorise any High Court to make any order on any other servant of the Crown as such merely to enforce the satisfaction of a claim upon the Crown", the learned Chief Justice answered that in the circumstances of this case the order was not being made merely for that purpose, but was being made for the purpose of ensuring that the orders of the Court were not ignored.

The intention of the learned Judges was to make an order requiring that the Commissioner "do forthwith proceed to deal with the case under sub-sec. 5 of s. 66 by setting aside the assessment and by repaying to the assessees the amount specified in the application". The formal order was made in the terms "that the first respondent do re-pay to the petitioners the sum of Rs. 3,17,187-8-0 with interest", etc. This part of the order is inartistically expressed: though it is true that in Sec. 49-A the phrase occurs "in lieu of payment of the refund," the duty of the Income-tax officials under the Act, and the duty of the Commissioner in the present case under Sec. 66, sub-sec. 5 was to record or cause to be recorded, an order allowing the refund to the assessees and to issue to them a refund order upon which they could obtain payment from a branch of the Treasury or of the Imperial Bank of India. While their Lordships do not say that the distinction between doing these acts and "repaying" is as important for the present purpose as it would have been in an English case (*cf. The Commissioners for Special Purposes of the Income Tax* v. *Pemsel*) it is very necessary that orders made under the Specific Relief Act should specify with exactitude and clarity the specific act which the person holding a public office is being commanded to do. Moreover, their Lordships cannot agree with the view taken by the High court that the Commissioner was obliged to discontinue proceedings against the Bombay Company as agent of the Hong Kong Company in respect of the year of assessment 1928-29. It was within the jurisdiction of

the Commissioner to direct further enquiry if he thought such enquiry to be reasonable and to be profitable in the public interest. Under Sec. 33 (2) he has a general power to make enquiry or to cause an enquiry to be made. It was certainly unfortunate that his order for further enquiry took the form of quoting the power given to Assistant Commissioners by clause (b) of sub-sec. 3. of Sec.31. That is one of several powers mentioned in the sub-section each of which is to be used in a proper case. As the whole question at issue was whether or not the Hong Kong Company, or the Bombay Company as its agent, were liable to be assessed at all, to direct the Income tax Officer to make a fresh assessment after making such further enquiry as he thought fit was an inappropriate form of order. But in substance the Commissioner was within his rights in directing further enquiry, and however disappointing this course may have been to the assessees, it is a matter which a Court of law must leave in the discretion of the Commissioner. The learned Judges of the High Court were not justified in thinking that this part of the order of the Commissioner was open to the criticism that the Commissioner was flouting or ignoring the High Court's decision.

Their Lordships cannot but agree, however, with the comments made by the learned Chief Justice upon the Commissioner's order of January 16, 1934, imposing as a condition of refund that Messrs. E. D. Sassoon & Company, Limited, should undertake to be responsible for paying back the amount in case an assessment were levied again or the matter was taken on appeal to the Privy Council. So, too, in the case of the order of the Income tax Officer, dated February 20, 1934, making an assessment in default under Sec. 23 (4) for failure to comply with the order of January 30, requiring the Bombay Company to produce the Hong Kong Company's books of account on February 15, the strictures of High Court are plainly justified. To this their Lordships will add that the action of the Income tax Officer in refusing to deal with the application under Sec. 27 until the disposal of the appeal to His Majesty in Council was equally open to criticism. Whether it adds to or subtracts from the discredit of such proceedings, if it be supposed that the Income tax authorities considered themselves entitled to do what was neces-

sary to retain the assessee's money until the decision of this Board could be obtained, is a question upon which no opinion need here be ventured. It should suffice now to observe that since August, 1934, the Income tax authorities have been withholding from the Bombay Company over three lacs of rupees extracted from them by an illegal assessment order, and that there is no pretence of justice or law in the notion that the money can be withheld in case on some future date a valid assessment may come into existence.

The action taken by the High Court under the Specific Relief Act was, however, incorrect. In the first place the decision of the Court upon the particular question referred to it in this case given in its special jurisdiction under Sec. 66 of the Act was "advisory": *Tata Iron and Steel Co.* v. *Chief Revenue Authority.* The complaint that the orders of the Court were being ignored does not appear to their Lordships to be a correct statement of the assessee's grievance. But in any case cl. (*g*) in Sec. 45 of the Specific Relief Act does not mean that orders can be made to enforce the satisfaction of a claim upon the Crown provided that the Court acts with some additional motive or has some further intention. The words of the clause have been taken *verbatim* from a well-known judgment on mandamus, the judgment of COLERIDGE, J., in *Baron De Bode's case*: "But, against the servants of the Crown, as such, and merely to enforce the satisfaction of claims upon the Crown, it is an established rule that a mandamus will not lie. I call this an established rule. I believe it has never been broken in upon". The doctrine is well illustrated by that decision and by the cases therein mentioned, but is even more fully expounded in *Regina* v. *Lords Commissioners of Treasury.* The principle is that the Court cannot claim even in appearance to command the Crown, and where an obligation is cast upon the principal the Court cannot enforce it against the servant merely as such. Before mandamus can issue to a public servant it must, therefore, be shown that a duty towards the applicant has been imposed upon the public servant by statute so that he can be charged thereon, and independently of any duty which as servant he may owe to the Crown, his principal. Whether the Commissioner of Income-tax, either gener-

ally or under Sec. 66, sub-sec. 5, of the Income Tax Act, is in this position as regards the refund of tax paid under an invalid assessment is the question raised by cl. (*g*) of Section 45 of the Specific Relief Act. This their Lordships do not find it necessary in the present case to decide; nor do they discuss the question whether in view of what LORD PHILLIMORE said in *Alcock Ashdown and Co. Ltd.* v. *Chief Revenue Authority* the assessees were in any difficulty by reason of Section 106 (2) of the Government of India Act, or had any other specific and adequate legal remedy: (*cf.* cl. (*d*) of Section 45 of the Specific Relief Act, Section 67 of the Income Tax Act, Section 32 of the Government of India Act). Before the assessees had brought their application on August 23, 1934, there was in existence the order under Section 49-A based upon the fresh assessment of February 20. To get rid of that order it was necessary that proceedings should be taken under Section 27, and it was not open to the assessees to apply to the Court direct for an order setting aside that assessment or the set off made thereunder. The assessee's application had contained cls. (*b*) and (*c*) whereby an order was asked directing the Assistant Commissioner to dispose of the appeal and the Income tax Officer to dispose of the application under Section 27. No order was made by the learned Judges of the High Court in respect of cl. (c) of the application and their Lordships do not consider that it was open to the learned Judges of the High Court to direct a refund to be made, or the necessary steps to be taken in that regard, so long as the fresh assessment stood. Their Lordships are, therefore, of opinion that the order of the High Court dated September 19, 1934, should be set aside and that the parties should pay their own costs of that application. They will humbly advise His Majesty to that effect and that subject thereto this consolidated appeal should be dismissed.

The Commissioner of Income tax, Bombay Presidency and Aden must pay to the Bombay Trust Corporation, Limited, two-thirds of their costs, in the consolidated appeal.

Appeal dismissed.

Solicitor for the Appellants:—*Solicitor, India Office.*
Solicitor for the Respondents:—*Linklater* and *Paines.*

[IN THE HIGH COURT OF MADRAS.]

THE SECRETARY OF STATE FOR INDIA

v.

V. M. MEYYAPPA CHETTIAR.

VARADACHARIAR AND STODART, JJ.

May 1, 1936.

JURISDICTION OF CIVIL COURT—SUIT TO DECLARE ASSESSMENT ILLEGAL ON THE GROUND THAT ASSESSEE WAS NOT RESIDING IN BRITISH INDIA—MAINTAINABILITY—FINALITY OF DECISION OF INCOME TAX AUTHORITIES ON THE QUESTION OF RESIDENCE—ABSENCE OF OTHER REMEDY—EFFECT—INDIAN INCOME TAX ACT (XI OF 1922), Secs. 4, 53 (4), 30, 67.

In respect of matters which the Income Tax Act has left to be determined by the income tax authorities their decision cannot be questioned by a suit in the Civil Court.

The plaintiff who was assessed to income tax in British India on the income received by him from his business in Saigon (Burma) instituted a suit for a declaration that he was not liable to be assessed under the Indian Income Tax Act inasmuch as he was not a resident of British India but was permanently residing in French territory when the income accrued to him. The income tax authorities had found after proper enquiry that he was residing in British India during the period in question and had assessed him to income tax accordingly: Held, *that the assessing authorities had power to determine the question whether the plaintiff resided in British India, and as they had found after due enquiry that he was a resident of British India, the Civil Court had no jurisdiction to entertain the suit.* Held, *further, that the fact that the assessee had been assessed under Sec. 23 (4) and had no other remedy would not give him a right to maintain a suit of this nature in the Civil Court.*

[Case law discussed].

Appeal against the order of the Court of the Subordinate Judge of Devakotta dated 25th January 1934 made in Appeal

Suit No. 36 of 1933 preferred against the decree of the Court of the District Munsif of Devakotta in O. S. No. 236 of 1931. [A.A.O. No. 99 of 1934].

The facts are stated in the judgment.

The Government Pleader for the Appellant.

K. Rajah Iyer and *V. Ramaswami Iyer* for the Respondent.

VARADACHARIAR, J.—This appeal arises out of a suit for a declaration that the plaintiff is not liable to be assessed to income tax on the income received by him from his business in Saigon and for recovery of tax levied from him for the years 1929-30 and 1930-31. The first issue in the case raised the question whether the suit was not barred by Section 67 of the Income tax Act, XI of 1922. Dealing with this point as a preliminary issue, the District Munsif dismissed the suit as barred by that section. The Lower Appellate Court was of opinion that the suit would be maintainable if the assessment was *ultra vires* or had been made without jurisdiction. In view of the allegations in the plaint, it held that the court must decide on evidence whether the plaintiff was permanently residing in French Territory, as, in that case any income there received by the plaintiff from the Saigon business would not be income assessable under the Act. It recorded a concession by the plaintiff's vakil that issue (6) in the case, *viz.*, "Whether the assessment was made without giving the plaintiff an opportunity to prove his contentions" could not be tried by the civil court. Issue (5) (a) raised the question of fact, "whether the plaintiff had ceased to reside in British India, and whether he had no assessable income in British India". The other issues were consequential. The lower appellate court accordingly remanded the suit for trial of issue 5 (a) and for findings on the other issues in the light of the finding that may be come to on issue 5 (a). Against that order of remand, this appeal has been preferred by the Secretary of State.

In view of the arguments urged before us, it is necessary to refer to a few facts appearing from the documents put in evidence as bearing on the preliminary issue. The plaintiff was at one time admittedly a resident of Palavangudi in the Chettinad (Ramnad District) but his case was that from 1926 he had been

permanently residing at Pondicherry in French territory and that after a partition in his family in 1928, he had no proprietory interests, business or assets anywhere in British India. In October 1929 the plaintiff's agent appeared before the Income-tax Officer and put forward this contention. For reasons recorded in Exhibit I, that officer declined to accept that plea. He was of opinion that the plaintiff's residence out of British India was only temporary, that his wife was living in Chettinad and that he had a right to share in the family house in Chettinad after his father's death. An appeal against Exhibit I proved infructuous; and as the plaintiff did not make any return in respect of his income or produce his accounts in spite of several adjournments, he was assessed under Section 23 (4) of the Act on a sum of Rs. 8,100, being the amount disclosed by the accounts of the partnership to have been remitted to him: (Vide Exhibit II).

For the next assessment, there was no appearance by or on behalf of the plaintiff before the Income Tax Officer. The steps taken to serve notices on the assessee are detailed in Exhibit III. On default of appearance in spite of these steps, the assessment had again to be made under Section 23 (4). But as, in the meanwhile, the assessee had sent a notice of suit to the Commissioner of Income Tax on 26-11-1930, the Income-tax Officer referred in his order (Exhibit III) dated 4-3-1931 to the materials on which he came to the conclusion that the plaintiff must be regarded as residing in Palavangudi. In addition to the circumstance stated in Ex. I, he referred to the fact that the plaintiff's wife was living in Palavangudi in a house which he believed was purchased by the plaintiff in her name and that from an affidavit filed by that wife it appeared that plaintiff celebrated his daughter's marriage in that house in the year *Sukla* (1929-30) and that the plaintiff occasionally used to come and stay with her in that house.

In the circumstances above stated, two contentions have been urged before us in support of the Government's appeal: (i) that the bar enacted by the first part of Section 67 of the Income-tax Act of 1922 is absolute and unqualified; and (ii) that the legislature had left it to the income-tax authorites to decide both questions of fact and law, that appropriate remedies by

way of appeal and reference (including a reference to the High Court on points of law) have been provided in the Act and that it could not therefore be the intention of the legislature that civil courts should in a separate suit be at liberty to examine the *correctness* of the conclusions arrived at by the Income-tax authorites.

Before dealing with the decisions cited before us, it is necessary to emphasise the fact that, in some of them, the question of exclusion of the Civil Court's jurisdiction had to be dealt with merely on general principles and in the absence of a statutory prohibition, while in others the decision turned upon the scope of the prohibition, enacted by statute. In the former class of cases, reliance has naturally to be placed on the *general scheme* of the law creating or empowering the authority whose acts are sought to be challenged. The observations of the Judicial Committee in *The Colonial Bank of Australia* v. *Willan* (L. R. 5 P. C. 417) are frequently referred to, as defining the limits of the civil court's powers of intervention. But even in applying these observations, it seems to me unwarranted to assume that in all cases in which a prerogative writ can, according to those observations, issue from a superior court, there must also exist a right of civil suit in the ordinary courts of the land.

Whenever the right sought to be vindicated is not a creature of the statute itself but a common law right relating to the person or property of the subject, courts start with the presumption that there must be a remedy in ordinary courts and insists on every clear and unmistakable indications of an intention to curtail or exclude the same ; and in this connection a distinction has been formulated between questions affecting the jurisdiction of the statutory authority and matters affecting the correctness of its decision. Even under the head of jurisdiction, a further refinement has been recognised, as indicated in the Judgment of Lord ESHER in *Queen* v. *Commissioners for Special Purposes of the Income tax* (21 Q. B. D. 319), according as the statute in question does or not entrust to the statutory authority itself jurisdiction to determine whether or not the preliminary state of facts essential to give it jurisdiction to act under the statute exists. In *Reg* v. *Belton* (1 Q. B. 66) which is referred to with approval in L. R. 5 P. C. at page 443 and numerous later decisions, it was

observed that the test of jurisdiction (for this purpose) was whether or not the authority in question "had power to enter upon the enquiry, not whether its conclusions in the course of it were true or false." The court explained the principle by adding that it might be shown that the tribunal had no authority to commence the enquiry "inasmuch as the question brought before them was not one to which their jurisdiction extended;' and this, although by mis-statements they have made the proceedings on the face of them regular."

In cases where the relevant statute contains a specific provision limiting or excluding the jurisdiction of civil courts, the determination of the ambit of civil court's jurisdiction must *prima facie* rest upon the language used in the excluding provision. Even here, when the language is not sufficiently definite or comprehensive, its interpretation is naturally influenced by the presumption against the intention to oust the jurisdiction of civil courts, especially when personal liberty and rights of property are concerned. One well known class of cases where the statute law has advisedly enacted only a restricted exclusion of civil jurisdiction is that relating to taxation by local or municipal bodies. (Cf. Section 354 of the Madras District Municipalities Act of 1920 and Section 228 of the Madras Local Boards Act of 1920 which preclude the challenge in a civil court of any assessment etc., *provided* that the provisions of the Act have been in substance and effect complied with). The result of such language is practically to assimilate this class of cases to those where the statute contains no *express* words of exclusion of civil courts' jurisdiction [cf. *Navadip Chandra Pal* v. *Purnananda Saha* (3 C. W. N. 73) and *Chairman, Giridhi Municipality* v. *Sirish Chundra Mozumdar* (I. L. R. 35 Cal. 859) which turned on Section 116 of the Bengal Municipal Act which merely said that no objection shall be taken to any assessment or rating in any other manner than in this Act provided].

Even where the words of exclusion in the statute are positive enough to exclude a writ of *certiorari*, the Judicial Committee made a reservation in (L. R. 5 P. C. 417) in respect of manifest defect of jurisdiction or fraud of the party. Whatever may be the disinclination of the legislature in England against enacting a total exclusion of the civil courts' authority or of English courts

in inferring it, such exclusion is not unknown in this country. The decision in *Spooner* v. *Juddow* (4 M.I.A. 353) is an instance in point. (See also *Govindarajulu Naidu* v. *Secretary of State*, I. L. R. 50 Mad. 449). The point for decision in 4 M. I. A. 353 related to the immunity of officers acting in excess of their powers in the administration of revenue law, similar to that provided for in the 2nd part of Section 67 of the Income tax Act; but their Lordships' observations, it was said, are equally apposite to the question arising under the first part of the section. The case is of special significance in view of the strong opinion expressed by Sir Erskine Perry (in the Supreme Court) in favour of the maintainability of the action. The learned Chief Justice referred to the interpretation placed by the Judicial Committee in *Calder* v. *Halket* (2 M.I.A. 293) on 21 Geo. III, c. 70, Sec. 24 and added 'if jurisdiction does not exist in the Supreme Court to correct wrongs of this kind, it exists nowhere': (see footnote on page 362 of 4 M. I. A. 353, Mr. Sanjeeva Row's edition of the Indian Reports). And yet their Lordships held against the jurisdiction of the Supreme Court, adding, "whether the plaintiff might have redress before any other tribunal can only be material in a doubtful construction of the statutes." If the jurisdiction of the Court is clearly taken away 'our decision' they said 'could not be influenced by the consideration that the plaintiff is left without remedy.'

In *Venkataratnam* v. *Secretary of State for India* (I. L. R. 53 Mad. 979) the exclusion of jurisdiction by Section 110 of the Government of India Act, 1915, has been held to exclude even the jurisdiction to issue a writ of *certiorari*. Whether the High Court can issue a writ of *certiorari* on an Income tax Officer in the mofussil, is a question beset with greater difficulty [see *In re Nataraja Ayyar* (I.L.R. 36 Mad. 72) and C.M.P. 2544 of 1935]; but one cannot on that account recognise a right of suit in contravention of the declared policy of the Legislature.

In the interpretation and application of taxing statutes, the distinction between liability to assessment and the method or quantum of assessment has long been recognised in the Land Revenue law of this country. After a review of the relevant statutory provisions, it was pointed out by a Full Bench in *Fahamidannissa Begum* v. *The Secretary of State for India*

in Council (14 Cal. 67 at page 84) that the former question had always been treated as and declared to be a matter for courts of justice. The same distinction was recognised in Section 58 of the Madras Revenue Recovery Act which excludes from the cognisance of Civil Courts only—questions as to "rate of land revenue or as to the amount of assessment." In 14 Cal. 67 the question was raised whether any and what departure had been made from this underlying principle by Act IX of 1847, either by reason of its general scheme or by the specific provision in Section 9 which enacted that 'no suit or action in any courts of justice shall lie against the Government or any of its officers on account of anything done in good faith in the exercise of the powers conferred by this Act.' The majority approached this question from the point of view that because of the declared policy of the Indian Legislature for at least 66 years, they should not adopt a construction involving a departure from it unless the Legislature had expressed such intention in clear and unmistakable language. As regards Section 9, they held that it only referred to suits for damages. This method of approach was approved of by the Judicial Committee on appeal in *The Secretary of State for India in Council* v. *Fahomidannissa Begum* (I.L.R. 17 Cal. 590) and with reference to Section 9, their Lordships observed "full effect can be given to this section without holding that it deprives the owner of a permanently settled estate of that right of appeal which is given to him in order that he may have determined in a Civil Court the justness of the demand of the Revenue authorities." The language of Section 9 was in effect limited by their Lordships in view of the previous state of the law and they added (on page 605) "if it had been intended to take away from the proprietors of estates the power by application to the courts to obtain immediate redress in any case in which the revenue authorities shall violate or encroach on the rights secured to them by the permanent settlement, it would have been done in express terms and not by such enactments as are contained in the Act of 1847."

Pausing for a moment, to compare Section 9 of Act IX of 1847 with Section 67 of the Income tax Act, 1922, I may point out that the exclusion in the Income tax Act cannot be explained away as relating only to suits for damages, because the section

consists of two parts, of which the latter alone may be said to correspond to Section 9 of Act IX of 1847. The first part in terms provides that no suit shall be brought in any civil court to set aside or modify any assessment made under this Act". Subject to the controlling effect of the words 'made under this Act,' here can be little doubt that the exclusion of the jurisdiction of the civil court is almost absolute. Can it be suggested that there is anything in the history of this branch of law which, as in the case of land revenue law, would justify the court in limiting the scope of this exclusion? I am not aware of any such consideration.

On the other hand, in the English system from which the income tax law has been borrowed, it was settled as early as in *Allen* v. *Sharp* [(1848) 2 Ex. 352] that legislative policy as well as considerations of expediency pointed to the propriety of treating the assessment by the assessing authorities as final and conclusive unless appealed from in the manner pointed out by the Statute. It is true that in *Kensington Income tax Commissioners* v. *Aramayo* [(1916) 1 A.C. 215 affirming the decision in *Rex* v. *Kensington Income tax Commissioners* (1914) 3 K.B. 429 at 447] it was decided that 'Prohibition' will lie and is an appropriate remedy if the Commissioners acted without jurisdiction. The case there was clearly within the principle of *Reg* v. *Bolton* (supra) because, according to the law, only certain specified Commissioners could assess a person to income tax in respect of profits derived from foreign possessions. Even on the facts found or assumed to exist, the court held that the particular Commissioner whose proceedings were sought to be restrained had no jurisdiction to proceed with the assessment, as he admittedly was not one of those specified in the Acts as competent to deal with such profits. The sense in which that decision must be understood was explained in *The King* v. *Bloomsbury Income tax Commissioners* [(1915) 3 K.B. 768]. When it was argued that the Commissioners had no jurisdiction to make or proceed upon the assessment, because, according to the petitioner's contention, he was not chargeable to income tax, and it was further contended that the Commissioners could not give themselves jurisdiction to assess a person by determining in the first instance that he was chargeable when in fact he was not, the Lord Chief

Justice (*Lord Reading*) reviewed the history of the income tax law and after referring to *Allen* v. *Sharp* [1848, 2 Ex. 352] held that "the scheme of the legislature is to entrust the decision of the facts to a tribunal of persons specially selected for the locality......................reserving always to the individuals the right to have the Commissioner's decisions on points of law reviewed by the courts. The obligation is placed for reasons of expediency upon the person assessed to appeal to the Commissioners if he wishes to rid himself of an assessment which is, in his view, based upon wrong conclusions of fact". The only qualification added is that the assessing authorities should have materials before them on which they could honestly come to a conclusion against the assessee. "Once that conclusion is reached, it follows that they had jurisdiction to decide all questions of fact". Avory, J., observed that "in such a case, it is an erroneous application of the formula to say that the tribunal cannot give themselves jurisdiction by wrongly deciding certain facts to exist, because the legislature gave them jurisdiction to determine all the facts including the existence of the preliminary facts on which the further exercise of their jurisdiction depends". Both Avory, J., and Lush, J., make it clear that a writ of prohibition may issue if the assessing authority had never satisfied itself that a person was chargeable or had acted without any enquiry or if its belief was founded on an obvious and manifest mistake in law. Mr. Rajah Iyer referred to an observation of Shearman, J., in *Rex* v. *Swansea Income tax Commissioners*, (1925, 2 K. B. at page 260) to the effect that "there may be cases in which prohibition may be obtained where the applicant shows that he is not liable to the jurisdiction of the Commissioner at all". Read in the light of other decisions and of the remarks of the other learned Judges who took part in that very case, this observation can only refer to cases like (1916 1 A. C. 215) where even on undisputed facts or facts assumed by the Commissioner, they would have no jurisdiction.

Whatever might be said of the Indian Income tax Act of 1886, there can be little doubt that the Indian Acts of 1918 and 1922 must in view of their elaborate provisions and safeguards, be interpreted in the light of the principles above set forth as

underlying the English Income tax Law. As I have already indicated, it may be open to doubt whether an ordinary civil action will lie in all cases in which and in all circumstances under which a writ of *certiorari* or prohibition may issue from a superior Court. But it certainly cannot be said that an assessment may be challenged by a civil suit even in circumstances in which a writ of *certiorari* or of prohibition will not be available. According to the facts which have been set out at the commencement of this judgment, the present case is one in which the Assessing Officer did make an enquiry as to the facts relating to the plaintiff's residence in British India and there is no reason to think that he did not or could not honestly come to the conclusion that the plaintiff was a resident of British India (*cf. Rogers* v. *Inland Revenue, 1 Tax Cases 225*) and received in British India the income remitted from Saigon. In this view the plaintiff's suit must fail.

Mr. Rajah Iyer contended that according to the scheme of the Income tax Act, it must not be held applicable to a non-resident assessee who disputed his liability to be assessed and that it did not entrust to the Revenue authorities the right to decide the question of his liability and much less the right to decide it finally. I am not able to accept these contentions. In (1915) 3 K. B. 768 already referred to, it was laid down, on the authority of *Allen* v. *Sharp* that the procedure under the Act applied as much to a person who contended that he was not chargeable as to one who admitted that he was chargeable, but complained of the manner or extent of assessment. The provisions of Sections 42 and 44 A of the Indian Act clearly contemplate assessments being imposed on income accruing to non-resident foreigners and there is no reason why the assessing authority should not have the power to decide a disputed question of residence or receipt in British India for the purpose of clauses 1 and 4 of Section 4 if it could and must decide disputed questions under Sections 42 and 44 A. The notice under Section 22 clause (2) of the Act must be issued to all persons who, in the opinion of the Income tax Officer, are in receipt of an income liable to tax and if a person thus served disputes his liability, I think it is his duty to put forth his objection before the assessing authorities. Section 30 makes it clear that one of the grounds

of appeal contemplated by the Act is the assessee's denial of liability to be assessed under the Act. I see no reason to limit the scope of the denial there contemplated to the exceptions enumerated in Clause (3) of Section 4. That a denial of liability on the ground of non-residence may be raised in the course of assessment proceedings is shown by *Commissioners of Inland Revenue* v. *Lysaght*, (1928 A. C. 234 on appeal from (1927) 3 K. B. 55). See also *Rex* v. *Marylebone Income tax Commissioners* (18 Tax Cases 740). 1928 A. C. 234 also shows that in certain circumstances and subject to certain limitations the question of residence may be a question of law fit to be referred to the High Court for its opinion. [See also *Levene* v. *Commissioners of Inland Revenue*, [1928 A. C. 217]. Mr. Raja Iyer also contended that as the plaintiff did not appear before the Income tax Officer he could not have applied to the Assistant Commissioner under Section 30; but I fail to see how that circumstance can affect the construction of the Act as to the scope of the matters to be decided by the assessing authorities.

It is not necessary for the purposes of this case to decide whether the language of the Section 67 of the Act of 1922 is clear or comprehensive enough to exclude a suit even in cases like those instanced by Avory and Lush, JJ., in (1915) 3 K. B. 768 as fit cases for the Court's interference by writs of *certiorari* or prohibition. The answer to that question will in some measure depend upon the construction to be placed on the expression " made under this Act ", occurring in the section.

As observed by Muthuswami Iyer, J., in *Venkata* v. *Chengadu* (I.L.R. 12 Mad. 175) with reference to similar language in Section 59 of the Madras Revenue Recovery Act ' the section presupposes that certain proceedings were professedly taken under the Act and that there might be a valid claim to redress on the ground that they were not in accordance with the provisions of the Act.' The question (which was left open in that case) is whether the proceedings contemplated are those which are vitiated by mere errors of procedure or include those taken without jurisdiction. Later decisions relating to sales for arrears of public charges have proceeded not so much on the construction of this or like expressions but on the broad ground that sales not warranted by the statute are void and do not therefore

require to be set aside within the shorter period of limitation: *C. Balakrishnan Das* v. *Simpson* (I. L. R. 25 Cal. 833), *Marakkolundayammal* v. *Secretary of State for India in Council* (I.L.R. 55 Mad. 876). In *Fischer* v. *Twigg* (I.L.R. 21 Mad. at p. 368), a case under the District Municipalities Act, it was observed that 'an imposition which is expressly prohibited by the Act cannot be deemed to be made under the provisions of the Act'. The principle thus stated may perhaps be unexceptional but its application will not always be easy. Take for instance, the first exception provided for in clause (3) of Section 4 of the Income tax Act of 1922, *i.e.*, that in the case of property held in part in trust for religious or charitable purposes, the income applied thereto shall not be taxed. Suppose the income tax authorities on the materials before them held that only a certain amount has been so applied but the assessee contends that a large portion of the income has been applied for the purposes of the trust; could it have been intended that such a dispute might be agitated in a regular suit?

Turning for a moment to the language of Section 67 of the Income tax Act of 1922, it is obvious that the second part of the section relating to the immunity of Government and its officers must cover not merely acts authorised by the Statute but also acts done without jurisdiction but in the *bone fide* belief that they were authorised (cf. the fuller language employed in Section 1 of Act 18 of 1850). Mr. Rajah Iyer suggests that this wider import is to be derived from the expression 'intended to be done' in that part of the section, but it seems possible that the word 'intended' was used only to signify 'futurity' so as to preclude suits for injunction in respect of proceedings 'intended' to be taken by the income tax authorities.

Amongst the reported cases under the Indian Income tax Acts brought to our notice, the only instance in which the assessee's suit succeeded is the decision of the Bombay High Court in *Haji Rahmatullah Haji Pir Mahomed* v. *The Secretary of State for India* (92 I. C. 351). The decision turned on Section 39 of Act II of 1886 which was substantially in the same terms as the first part of Section 67 of the Act of 1922 and the learned judges categorically laid down that 'if the assessment is clearly *ultra vires* we do not think the provisions of that Act

will apply'. There was no further discussion of the question of jurisdiction and the rest of the judgment deals only with the propriety of the assessment. The ground of denial of liability in that case no doubt was that the profits did not arise or accrue in British India but the rival contentions would seem to have turned on a point of law, the facts not being in dispute; and the learned judges held that on the facts stated 'the profits accrued in the Baroda State'. The case is accordingly of no help to the present plaintiff, though it is an authority against a total denial of a right of suit. The Act of 1896 contained no provisions corresponding to the second part of Section 67 of the present Act which I have referred to above as throwing some light on the construction of the first part: nor did it contain the safeguards enacted in the present Act, by way of a right of appeal (under Section 30), reference to a Board of Referees (under Section 33A) and reference to the High Court with a right of appeal to the Privy Council, under Sections 66 and 66A. I am not prepared to assume that the existence of these provisions indicating an elaborate special procedure would have made no difference in the opinion of these learned judges.

In *In re Ramjidas Mahaliram* (62 Cal. 1011; 1936 I.T.R. 25), the discussion related to writs of certiorari and prohibition. The decision emphasises the significance of the fact that in the Act itself 'there is machinery by which the assessee may bring the matter before the Court and he can no longer contend that he has no specific or adequate remedy.' It is true that on page 1033 the learned Judge observes that it is not for the Income tax Officer to decide whether the state of facts contemplated by Section 34 exists and "if he reopens the assessment without their existence he is acting without jurisdiction." But the context suggests that the learned Judge made that observation with reference to the nature of the special provisions in Section 34; otherwise he would not have left unanswered the argument based on 21 Q. B. D. 313 and *King* v. *General Commissioners for Taxes for the District of Clerkenwell*, [(1901) 2 K. B. 879]. The remark that English decisions are not authoritative on the construction of the Indian Income tax Act was directed to the argument that the assessing officer's functions are only 'administrative' and not 'judicial.'

In *Secretary of State for India in Council* v. *A. H. Forbes* (A. I. R. 1922 Pat. 361) the actual decision was in favour of the Government, but the learned judge affirmed the principle that if a statutory authority purports to exercise its powers on what is not according to law the subject-matter of these powers the Court will interfere 'because the authority is not acting under the statute and is not protected thereby.' The reference to *Chairman of Giridhi Municipality* v. *Sirish Chander Mozumdar*, (12 C.W.N. 709; 35 Cal. 859) and the quotation made from that judgment suggest that the learned judge did not in the circumstances find it necessary to keep apart the two classes of cases in one of which the exclusion of the Civil Court's jurisdiction is enacted in much more restricted terms than in the other.

In *Rajah of Ramnad* v. *Secretary of State for India*, ((I.L.R. 52 Mad. at pages 17 and 18) it was no doubt stated that where a "certain income is outside the scope of the Act, such as agricultural income or income not earned in or brought into British India, any assessment in respect of such income would be outside the scope of the Act and a civil suit to recover it would not be barred"; but the observation was obiter and it became unnecessary to pursue the matter as the assessee's suit failed on another ground. Further, no reference was made to the possible distinction between cases in which the item of income was even on the admitted facts outside the scope of the Act and those in which the assessing authorities had to decide on evidence, whether it was within the Act or not. *Dayaram Ramdas* v. *Secretary of State for India*, (78 I.C. 940; A.I.R. 1925 Sind 130) likewise contains only a *dictum* that if the Income tax authorities had assessed anything but 'income' or had levied assessment on the classes of income exempted by the Act they would have overstepped the limits of their jurisdiction and the assessment would not have been under the Act. *Dr. R. N. Singha* v. *Secretary of State for India in Council*, (I.L.R. 5 Rang. 825) adds very little, beyond referring to the distinction between 'erroneous' assessment and '*ultra vires*' assessment.

In *Forbes* v. *Secretary of State for India* (I. L. R. 42 Cal. 151) there appears a concession by Counsel in the course of the argument (see page 153) that if the Collector assesses anything but income, he acts beyond his jurisdiction but on the

next page he is reported to have maintained that it is for the Collector to determine who is chargeable and that the Civil Courts have no jurisdiction to determine that question. The Judgment reflects this line of argument; it is however noteworthy that when counsel was referred to *Kameswar Pershad* v. *The Chairman of Bhabua Municipality*, (I. L. R. 27 Cal. 849) he pointed out what I have already indicated that the provisions of the Income tax Act are different from those of the Municipal Act. The learned Government Pleader claimed that I. L. R. 48 Cal. 151 was a direct authority in his favour even for the purposes of the present case, because he said, in both cases the question must be held to relate to the person chargeable; but this ignores the fact that in the Calcutta case the income was admittedly assessable whereas in the present case the income will not be within the Act at all if the plaintiff's contention as to his residence is true. The learned Judges however recognised the principle that in respect of matters which the Act has left to be determined by the assessing authorities, their decision cannot be questioned by a separate suit. As I have held that in the present case also, the assessing authority had power to determine the question of the plaintiff's residence in British India and the consequent receipt of the profits here, the plaintiff's suit must fail even according to the principle of the Calcutta decision.

The appeal is allowed and the plaintiff's suit is dismissed with costs throughout.

STODART, J.—This appeal arises out of a suit filed by the respondent Meyyappa Chetty in the Court of the District Munsif, Devakottai. The plaintiff is a merchant having a business in Saigon. He was assessed to income tax in British India on profits of this business brought into British India in the years 1929-30 and 1930-31. Such profits are chargeable only if they are received in or brought into British India in the years 1929-30 and 1930-31. Such profits are chargeable only if they are received in or brought into British India by a resident in British India. See Section 4, sub-section (2) of the Act. Plaintiff by his local agent contended before the Income tax Officer that he did not reside in British India, but the Income tax Officer found against him and required him under Section 22 to submit a return of his income. He did not do this and was assessed under Section 23, sub-section 4, and under Section 30 became debarred from the remedies provided by the Act: namely, from

the right of appeal to the Assistant Commissioner and second appeal to the Commissioner; and from the right conferred by Section 66 of having a reference made to the High Court. Incidentally it may be observed that plaintiff contended also that he had no property in British India, but he must have had some property which could be proceeded against for the realisation of the tax; for he paid the tax.

Plaintiff then filed this suit for a declaration that he was not liable to be assessed and to recover the tax paid by him. He contended that he was not a resident of British India but of Pondicherry in French India. He contended firstly, that the Income tax Officer had not conducted a proper enquiry into the question of his residence and that he had had no proper opportunity of stating his case on this point; and secondly, that the Income tax Officer was wrong in holding that he was a resident of British India. The first of these grounds is now given up. There is no doubt that the Income tax Officer did hold an enquiry as to the question of plaintiff's residence and decided that question to the best of his ability on the materials available. The learned District Munsif held that plaintiff's suit was not maintainable being barred by Section 67 of the Act, the first part of which is "No suit shall be brought in any Civil Court to set aside or modify any assessment made under this Act."

Plaintiff appealed to the learned Subordinate Judge of Devakottai who held on the contrary that if it was true that the plaintiff was not a resident of British India then the Income tax Officer's decision on that point was wrong and the assessment based on that decision was not made "under the Act" and so a suit to set aside that assessment lay; and in the result remanded the suit for trial of the issue "Whether the plaintiff had ceased to reside in British India and whether he had no assessable income in British India." Against that order of remand this appeal is preferred by the Secretary of State.

The learned Government pleader for the appellant contends that the question of respondent's residence was one which the Income tax Officer had jurisdiction to decide; that his decision on the point was thus made under the Act; and that it cannot be challenged by a suit in the ordinary civil court but only in the manner provided by the Act. Learned Counsel for the respondent

argues on the other hand that in deciding the point wrongly, the Income tax Officer wrongly assumed jurisdiction and the assessment which followed on that decision was without jurisdiction. My finding is that the appellant's case is supported by ample authority and that the appeal must succeed.

The respondent does not dispute the general principle that when the Legislature sets up authorities and tribunals to deal with a certain limited subject-matter then a person aggrieved by an act done or decision made by such tribunal must have recourse to the remedies provided by the statute unless the act or decision complained of is done or made without jurisdiction or is in excess of jurisdiction. In the latter case he has recourse to the Civil Court; his remedy in India being by way of suit, in England by one of the prerogative writs such as prohibition or *cretiorari.* See *Robertson's Civil proceedings by and against the Crown;* and *Halsbury's Laws of England* under the title Crown Practice, Chapters II to V, and the judgments of BANKES, L.J., and ATKIN, L.J., in *Rex* v. *Electricity Commissioners* [(1924) 1 K. B. 171] and more particularly the general observations of ATKIN, L.J., at page 204: "Wherever any body of persons having legal authority to determine questions affecting the rights of subjects and having the duty to act judicially act in excess of their authority they are subject to the controlling jurisdiction of the King's Bench exercised in these writs" (p. 205). The point which we have to decide in this appeal is whether the decision which the Income Tax Officer made as to the residence of the respondent was made in excess of his authority. A question of that kind must obviously arise in all cases in which under the Income Tax Act the taxing officer has to decide whether any particular item of income is or is not chargeable. I may observe also that the exempting clause in the Income Tax Act, namely, section 67, and similar clauses in other Acts which protect acts done and decisions made by statutory authority do nothing more than enunciate the general principle. For instance Section 67 protects assessments made "under the Act". It does not protect assessments made in excess of jurisdiction.

This general principle is well establised in decisions of the Indian Courts. See the judgment of MUKERJI, J., in *Chairman of Giridhi Municipality* v. *S. C. Mozumdar* (I. L. R. 35 Cal.

859), where the question for decision was the validity of a tax levied on property. "A corporation which is invested with authority to assess taxes, is really invested with quasi-judicial power, and though its action when taken in conformity with the provisions of the law which created the authority, may not be liable to challenge in the Civil Courts, it does not enjoy a similar immunity when that action can be challenged on the ground that it has been taken either in excess of or in contravention of the powers conferred upon it by the Statute" (page 865). The Bengal Municipal Act which was then under consideration contained an excluding clause (Section 116) to the effect that no objection could be taken to any assessment or rate in any other manner than in the Act provided and this clause was strongly relied on by the Municipality on whose behalf it was contended that regular suit for cancellation of the assessment was not contemplated by the Legislature. On this point MOOKERJI, J., said "In my opinion this contention is not well-founded upon principle, and is not supported by any authority. The effect of . . . . . Section 116 was considered in the cases reported at 1898 C. W. N. p. 73 and I. L. R. 27 Cal. 849. In these cases it was pointed out that Section 116 does not take away the jurisdiction of the Civil Court in a case in which it is alleged and established that the assessment is open to objection on the ground that it is *ultra vires*, in other words it is only when the action of the Municipality has been exercised in conformity with the powers conferred upon it by the Act that the Civil Court has no power to interfere". Again in a case in which the Standard Life Assurance Company sued the Municipal Council, Cocanada, to recover a sum levied on it as profession tax it was held (I. L. R. 24 Mad. 205) (1) that the suit lay because the Council had no authority to tax an insurance company, life insurance not being one of the businesses or trades in respect of which a tax might be levied and (2) that the suit was not barred by the excluding clauses, namely, section 101 of the District Municipalities Act, 1884. "The assessment or demand of any tax, when no appeal is made as hereinafter provided and the adjudication of an appeal by the Municipal Council shall be final" and Section 162 (2) "No suit should be brought in any Court to recover any sum of money

collected under the authority of the Act. . . . . . provided that the provisions of this Act have been in substance and effect complied with". Their Lordships say "The question really is whether when a company . . . . which is not taxable under the act, is nevertheless taxed, it can be said that the provisions of the Act have been in substance and effect complied with". In other words the immunity conferred on statutory authorities by the provision which shuts out the jurisdiction of the Civil Court does not extend to cases where their decisions are *ultra vires*.

The respondent here, as I have said, does not quarrel with the general proposition of law that the statutory authority is immune from suit so long as it acts in conformity with the statute and does not exceed its powers. What then is his position? It is this. Before proceeding to make the assessment the Income Tax Officer had to decide whether or not the assessee resided in British India. Having wrongly decided this in the affirmative he wrongly assumed jurisdiction. Therefore the assessment was made without jurisdiction and is not protected by the general principle; and is not protected by Section 67 either, since it was not made "under the Act". The question for decision therefore in this appeal is simply this: Had the Income Tax Officer jurisdiction to decide the point of the respondent's residence? Then, if he did so after proper enquiry—for absence of proper enquiry has always been held to impair jurisdiction—his action in making the assessment in pursuance of that decision was not wrong. I must observe again that though the respondent raised the plea of absence of proper enquiry in the trial court, he abandoned it on appeal. The whole case of the respondent therefore is that before proceeding to make the assessment, the Income Tax Officer had to find that the respondent was a resident of British India and having wrongly found that as a fact, he wrongly assumed jurisdiction to assess this particular item of income and thus acted without jurisdiction in assessing it.

Another point which arose in the course of the argument is this. Being a subject of a foreign state respondent claims to have been within his right in ignoring the requisitions of the Income Tax Officer that he should make a return of his income.

Section 30 of the Act debars him from the remedies provided by the Act. Is he therefore to have no redress in the courts of British India? As will be seen hereafter there is ample authority for the position that the absence of any other remedy is not to be taken into consideration in deciding the question whether the decisions of a statutory tribunal are or are not final. That a statutory tribunal or authority which has to arrive at a decision as to the existence or non-existence of certain facts before proceeding to take further action under the statute, is acting within its jurisdiction in making that decision and is immune from civil proceedings to quash that decision except such as are prescribed by the statute, is established beyond all controversy.

In *Rex* v. *Commissioners for Special Purposes of the Income Tax* (21 Q. B. D. page 313) the question arose on the interpretation of the words "at the end of the year". The Commissioners for General Purposes were empowered to grant certificates for refund of income tax overpaid, on application made "at the end of the year". Having done so in certain cases in which the applications were made long after the end of the year, the Commissioners for Special Purposes refused to honour the certificates on the ground that they were granted without jurisdiction. It was held that the Commissioners for General Purposes had jurisdiction to decide whether in the circumstances the applications were made in time. LORD ESHER (Master of the Rolls) dealing with this point observed: "When a tribunal or body which has to exercise the power of deciding facts, is first established by Act of Parliament, the Legislature has to consider what powers it will give that tribunal or body. It may in effect say that, if a certain state of facts exists and is shown to such tribunal or body, before it proceeds to do certain things, it shall have jurisdiction to do such things, but not otherwise. There it is not for them conclusively to decide whether that state of facts exists, and if they exercise the jurisdiction without its existence what they do may be questioned. But there is another state of things . . . . The Legislature may entrust the tribunal or body with a jurisdiction which includes the jurisdiction to determine whether the preliminary state of facts exists as well as the jurisdiction, on finding that it does exist, to proceed further or do something more . . . It is an erroneous application of

the formula, to say that the tribunal cannot give themselves jurisdiction by wrongly deciding certain facts, because the Legislature gave them jurisdiction to determine all the facts, including the preliminary facts on which the further exercise of their jurisdiction depends".

In a recent case *Rex* v. *Bloomsbury Income Tax Commissioners*, [(1915) 3 K. B. p. 768] where the question at issue was the legality of a surcharge made by the Commissioners on the report of a surveyor of taxes, it was contended on behalf of the applicant that the Commissioners could not give themselves jurisdiction by wrongly deciding that the applicant was chargeable. LORD ESHER'S finding in the case just cited was emphatically affirmed. LORD READING, C. J., said "In my judgment this *dictum* states accurately the principle applicable to such cases," and again

"In my view an examination of the Income tax Act shows that the scheme of the Legislature is to entrust the decision of the facts to a tribunal of persons specially selected for the locality, and who are often in a better position than the Courts to determine the questions of fact . . . . The exigencies of the State require that there should be a tribunal to deal . . . . with all such questions and to decide them finally. . . . . The obligation is placed for reasons of expediency, upon the person assessed, to appeal to the Commissioners if he wishes to rid himself of an assessment which is in his view based on wrong conclusion of fact, and this obligation rests equally upon a person who contends that he is not chargeable as upon a person who admits that he is chargeable but not to the extent of the assessment made upon him."

Rex v. *General Commissioners of Income Tax for Clerkenwell* [(1901) 2 K. B. 879] was an application to prohibit the Commissioners from assessing certain profit to income tax on the ground that by an erroneous decision on the facts they were seeking to give themselves a jurisdiction which they did not possess. It was held that they were merely deciding facts going to the quantum of taxable liability and that the proper remedy was by appeal upon a case stated; that is to say, the remedy provided by the statute. The Commissioners, having jurisdiction under the Income tax Act (1842) to assess a certain Company to income

tax in respect of profits of a business carried on either wholly, or in part only, in Great Britain, they had for the purposes of that assessment jurisdiction to decide all questions of fact necessary for ascertaining the amount of those profits, and therefore prohibition would not lie. What the Commissioners had decided was that the profits of the Eastern Kodak Company carrying on business in the United States were technically the profits of the Kodak Company which carried on business in London. The Court refused to enter into the merits of this decision.

Colonial Bank of Australia v. *Willan* [Privy Council Appeal Cases Vol. V (1873-1874) p. 417] is an interesting and authoritative case which is relevant here on two grounds. The appeal was brought from a judgment of the Supreme Court of Victoria which quashed an order made by a Court of Mines established under a statute called the Mining Statute. The order of the Court of Mines was that a certain company should be wound up forthwith under the provisions of the Mining Companies Limited Liability Act; and was made at the instance of the Colonial Bank on the ground that the company owed it a large amount of money. The Supreme Court having been moved by writ of *certiòrari* rescinded the order on the ground that it was made without jurisdiction as the company was not indebted to the Bank, which again depended on the question whether the debt was incurred with the authority of duly constituted officers of the company. The Judicial Committee held that the question of the existence of the debt was a question which the Judge of the Court of Mines was competent, in fact, bound to decide, that the Supreme Court could only come to the opposite conclusion upon a retrial of the question (which of course was inadmissible); and that the winding up order could not therefore be quashed on the ground that it was made without jurisdiction. See page 443: "An objection that the Judge has erroneously found a fact, which though essential to the validity of his order, he was competent to try, assumes that having general jurisdiction over the subject-matter, he properly entered upon the inquiry but miscarried in the course of it. The Supreme Court cannot quash an adjudication upon such an objection without assuming the functions of a Court of Appeal, and the power to retry a question which the Judge was competent to decide." The second point on which

this decision is relevant to the present case arises from the fact that the Mining Statute contained a clause providing that no proceedings under the Act should be removed or removable to the Supreme Court save as provided in the Act. The Judicial Committee held that this preventive clause did not operate to deprive the Supreme Court absolutely of its power to issue a writ of *certiorari*, but merely controlled and limited its action on such writ: and expressed its opinion that in such cases the Court would interfere to quash an order only upon the ground of manifest defect of jurisdiction in the tribunal making it, or of manifest fraud in the party procuring it. See *Halsbury*, Vol. 9, page 862, para. 1458, in the title Crown Practice. "Although *certiorari* is taken away (by the statute) it may be granted when the inferior Court has acted without or in excess of jurisdiction, for in such a case the Court has not brought itself within the terms of the Statute taking away *certiorari*." This is the exact position contended for by the respondent here. Section 67 does not bar a suit to set aside an assessment made without jurisdiction for the reason that such an assessment is not made under the Act.

The second main contention of the respondent is that being a foreign national he was entitled to ignore the requisitions made by the Income Tax Officer calling upon him to make a return of his income under Section 30 of the Act. Having thus become debarred by the remedies provided by the Act by way of appeal and second appeal etc., he is left without remedy unless he can file a suit against the Government to establish that he is not assessable to income tax. The fact that a person has no other remedy has however been held by the highest authority to be no answer to the objection that no action lies in the ordinary Civil Courts to challenge the act of a statutory authority so long as the latter acted within his authority. In *Spooner* v. *Juddow* (4 M. I. A. p. 353) which was an appeal by a Collector of Revenue against a decision of the Supreme Court of Bombay mulcting him in damages in an action for trespass, it was held by the Judicial Committee that the action was barred by XXI Geo. III, c. 70, s. 8: "That the said Supreme Court shall not have or exercise any jurisdiction in any matter concerning the revenue etc." It was also held, on the argument that the respondent had no other remedy as follows: "Whether the plaintiff

might have redress before any other tribunal can only be material in a doubtful construction of the Statutes and Charters establishing the Court in which the action was brought. If by these Statutes and Charters its jurisdiction is clearly taken away, our decision could not be influenced by the consideration that the plaintiff is left without remedy.

There is always a remedy of course for acts done or decisions made under colour of any particular statute when these acts are done or decisions are made without jurisdiction or in excess of jurisdiction. MUKERJI, J., in *Giridhi Municipality* v. *S. C. Mozumdar,* cited above, indicates the particulars in which the jurisdiction of the quasi judicial tribunal may be defective or when it may be exercised in excess. (See page 866 of 35 Cal.). There may be a manifest defect of jurisdiction in the tribunal that made the order such as in the case reported in (1916) 1 A.C. page 215, where an income tax assessee was assessed by the Commissioners for Kensington when on the facts stated he should have been assessed by the Commissioners for the City of London. There may be manifest fraud in the party obtaining the order. There may be something defective in the character or constitution of the Court. Again the subject matter of the enquiry on which the decision was made may be outside the scope of the Act as in the *Standard Life Assurance Company* v. *Municipal Council, Cocanada,* cited above. There may be the absence of some preliminary proceeding which was necessary to give jurisdiction to the tribunal. For example take these cases where revision of property tax in a Municipalitiy is challenged on the ground that the prescribed formalities of publication etc., were not observed. The cases cited by the learned Counsel for Respondent are examples of these principles and are no exceptions to the general rule. In *H. R. H. Tarmahomed* v. *Secretary of State* (92 I. C. 351) the assessee had been assessed on profits which accrued in the native state of Baroda and were received by him in the native state of Gondal. Such profits are clearly outside the scope of the present Income Tax Act as they were outside the scope of the then existing Act II of 1886. On the facts of the case the Income Tax Officer had no jurisdiction and his fallacious reasoning that the profits were taxable because they accrued on the sale of grain which was grown in British

India and exported into Baroda was rejected. See also the observations of the learned Judges in *Raja of Ramnad* v. *Secretary of State for India* (I. L. R. 52 M. page 12) "if the tax was levied under the Act no doubt a suit would be barred but if the assesment was made in respect of an item of income which is not assessable under the Act, a civil suit would lie to recover it inasmuch as the officer making the assessment had no jurisdiction to make it. In cases in which the Income Tax Officer had to decide whether a certain item of income is assessable or not, his decision cannot be said to be *ultra vires* even if it is illegal. But where a certain income is outside the scope of the Act, such as agricultural income or income not earned in or brought into British India, any assessment made in respect of such income would be outside the scope of the Act; and a civil suit to recover it would not be barred by reason of S. 52." For the converse proposition that no suit will lie when the Income Tax Officer is acting within his powers in making the assessment see *Forbes* v. *Secretary of State* (42 Cal. page 151). That was a case where the plaintiff Forbes contended that he was not liable to be assessed on profits received by him as an executor. JENKINS, C. J., said "The Collector has come to the conclusion that the subject matter with which he was dealing was income, as admittedly it was, and so was subject to tax. He further determined that the plaintiff being the person to whom the income accrued was the person chargeable. In so determining he was exercising a jurisdiction that was clearly vested in him by the Act, and I cannot see how it can be said that he purported to exercise a jurisdiction which he did not possess and so did not make an assessment under the Act. This is income which is liable to be taxed within the meaning of the Act. The Collector has determined that the plaintiff is a person chargeable and in so doing has acted within the limit of his jurisdiction. That being so it appears to be a case where according to S. 39 (which in terms is the same as S. 67 of the present Act) it is right to say that the suit does not lie."

I agree therefore with my learned brother in holding that respondent's suit was not maintainable. This appeal is allowed with costs. The order of the Lower Appellate Court is set aside and the decree of the trial Court restored.

Appeal allowed.

[In The Lahore High Court.]

HARNAND RAI HARBHAGAT RAI
v.
COMMISSIONER OF INCOME TAX, PUNJAB AND N. W. F. P.

Sir James Addison and Abdul Rashid, JJ.

January 23, 1936.

Bad Debt—When Debt Becomes Bad—Sufficiency of Evidence—Absconding of Debtor, Effect of—Loan And Partnership—Indian Income Tax Act (XI of 1922), Sec. 10 (2) (ix).

The assessee advanced large sums of money to a contractor. On July 10, 1928, a sum of Rs. 24,388 was found due to the assessee and the parties agreed that this sum would be repaid by the debtor on receipt of cheques from the Government for work done. The excess or deficiency was to be borne half and half. After paying a small amount the contractor absconded. In the assessment of 1931-32 the assessee claimed deduction of the amount remaining due to him. The Commissioner disallowed deduction holding that the loss was a loss of capital in a partnership and that the debt had become bad in 1928:

Held, (1) *that there was no evidence to support the finding that the loss was not a loss incurred in the money lending business of the assessee but a loss in partnership*; (2) *that though the debtor absconded in 1928, the assessees had still three years to make up their mind whether to sue him or not: the debt could be said to have become bad only on 10th July 1931 and allowance should have been made for it in the year 1931-32.*

Case stated under Sec. 66 (2) of the Indian Income Tax Act by the Commissioner of Income Tax, Punjab and N. W. F. P. in the matter of the assessment of Messrs. Harnand Rai Harbhagat Rai for the year 1932-33.

Anant Ram Khosla for the Assessees.

Jagannath Aggarwal for the Commissioner.

ORDER.

The following two question were referred to this Court under Section 66 (2) of the Indian Income Tax Act on behalf of the firm Harnand Rai Harbhagat Rai, Multan, by the Commissioner of Income Tax, Punjab, North West Frontier and Delhi Provinces, Lahore:

(1) Whether there was proper and material evidence before the Income Tax authorities to disallow Rs. 27,768 claimed as a bad debt in the account of Haji Sikandar Khan.

(2) Whether, on the facts of the case, Section 26 (1) or Section 25 (3) was applicable?

It was claimed in the assessment of 1931-32 that the sum of Rs. 21,768 should be allowed as a bad debt. The Income Tax Officer disallowed the claim on the grounds that it was a partnership loss which had not been proved, and that the debt had not yet become bad in the relevant account year, that is 1930-31. An appeal was preferred against this decision but eventually the amount was left over for future consideration under Section 33. The claim was repeated during the assessment of 1932-33 but it escaped the notice of the income tax officer who passed no orders on it. It was however, before the Assistant Commissioner in appeal. He disallowed the claim and the matter then came before the Commissioner.

Large sums were undoubtedly borrowed by Haji Sikandar Khan from the assessee firm. The final adjustment between them took place on the 10th of July 1928 when a sum of Rs. 24,388 was found due by Haji Sikandar Khan. The parties came to an agreement about this to the effect that this sum would be repaid to the assessee firm by Haji Sikandar Khan on receipt of cheques from the Government. If the cheques were less than the amount or in excess of the amount the loss or the excess was to be divided between them, that is to say, if the cheques came to more than Rs. 24,388 the assessee firm was to get half the excess and if they were less, the assessee firm was to bear half the loss. A small amount was recovered by cheques bringing the total balance down to Rs. 21,768 and then Haji Sikandar Khan, who was a contractor and had come from Kabul, went back to Kabul without paying any of the other cheques received from Government.

The Commissioner is of opinion that the nature of the advances without any security and without any stipulation for interest conclusively suggests a contractual relationship between the assessees and the debtor. He was further of opinion that this received corroboration from the language of the final agreement which I have already given. He therefore came to the conclusion that this loss was a loss of capital belonging to the assessee firm which had been invested by it in Haji Sikandar Khan's business. He was also of opinion that the loss was not allowable under Section 10 (2) (ix) as it was not a loss pertaining to the money lending business and did not take place in the relevant year but in 1928.

On the record we find no evidence to establish that this was not a loan but capital invested in Haji Sikandar Khan's business. The final agreement does not help to prove this. The assessee firm knew that it was not likely to get more than the Government cheques as Haji Sikandar Khan belonged to Kabul and not to Multan where he was doing contract work. By the agreement in question it stood to gain if the Government cheques were more than the debt due and if they were less they had in any case little or no chance of recovering the balance. The other evidence consists of the accounts and no inference can be drawn from them. We therefore hold that there was no evidence before the Income Tax authorities to establish that this was not a loss pertaining to the money-lending business but was a loss of capital invested in Haji Sikandar Khan's business.

Further it cannot be said to have become a bad debt in 1928. Haji Sikandar Khan absconded, it is true, in that year but the assessee firm had three years to make up their minds as to whether it was worth while suing him. It was not therefore till the 10th of July 1931, that it could be said that this was a bad bebt. Had he come back before that and started contracting business in India, the assessee firm would probably have sued him for the amount but it would have undoubtedly been premature to wipe out this debt as bad prior to the 10th of July, 1931. It became a bad debt actually in the account period under discussion, namely, on the 10th July, 1931, and an allowance should have been made for it under Section 10 (2) (ix) by the Income Tax authorities. For these reasons we answer question No. 1 in the negative.

The counsel appearing for the assessee firm stated that he no longer pressed the matter raised in question No. 2. It is not therefore necessary for us to give a reply to it.

We think in this case that the assessee firm should get its costs from the Commissioner.

Reference answered accordingly.

[IN THE CALCUTTA HIGH COURT.]

P. C. MALLICK and D. C. AICH, *In re.*

DERBYSHIRE, C.J. and COSTELLO, J.

March 3, 1936.

EXECUTORS—LIABILITY TO PAY INCOME TAX—DEDUCTIONS—COST OF OBTAINING PROBATE OF WILL—AMOUNT DIRECTED TO BE PAID OUT OF INCOME FOR PERFORMANCE OF TESTATOR'S *Addya Sradh*—INDIAN INCOME TAX ACT (XI OF 1922), SECTIONS 7 TO 12.

Executors are liable for income tax in respect of the income received by them in their capacity as executors.

The cost of obtaining probate of the will of the testator cannot be excluded from the chargeable income of the executors even though there is an express provision in the will that the same shall be payable out of the income of the estate.

Where a testator had directed his executors and trustees to pay Rs. 10,000 for the expenses in connection with his addya sradh *to the person who would be entitled to perform the* sradh, *out of the income of his property, and an amount of Rs. 5,537 was actually spent on the* addya sradh, *in the year of account :* Held, *that in computing the chargeable income of the executors, neither the entire sum directed to be paid to the person entitled to perform the* sradh *nor even the amount actually spent thereon can be deducted.*

These are not cases of allocation of a sum out of the revenue before it becomes income in the hands of the executor but are cases of

the application by the executor under the direction of the testator of a part of the income in his hands in a particular way.

A. H. FORBES *v.* SECRETARY OF STATE FOR INDIA IN COUNCIL *and* TRUSTEES OF SIR CURRIMBHOY EBRAHIM BARONETCY TRUST *v.* COMMISSIONER OF INCOME TAX, BOMBAY, *applied.*

BEJOY SINGH DUDHURIA *v.* COMMISSIONER OF INCOME TAX, BENGAL, *distinguished.*

Cases referred to:

FORBES *v.* SECRETARY OF STATE [1915] (I.L.R. 42 Cal. 151; 19 C.W.N. 138; 29 I.C. 893; 1 I.T.C. 8).

COMMISSIONER OF INCOME TAX, BOMBAY *v.* TRUSTEES OF CURRIMBHOY EBRAHIM BARONETCY TRUST [1934] (61 I.A. 209; 2 I.T.R. 148; 58 BOM. 317; 148 I.C. 855; A.I.R. 1934 P.C. 116; 38 C.W.N. 618; 36 BOM. L.R. 557).

BEJOY SINGH DUDHURIA *v.* COMMISSIONER OF INCOME TAX, BENGAL [1933] (60 I.A. 196; I.L.R. 60 CAL. 1029; 35 BOM. L.R. 811; 143 I.C. 145; 1 I.T.R. 135).

The material facts are stated in the judgment.

C. C. Biswas and *S. C. Ghose*, for the Assessees.

The Advocate-General and *Romesh Chandra Pal*, for the Income Tax Department.

DERBYSHIRE, C.J.—This is a Reference under Section 66 (*1*) and 66 (*2*) of the Indian Income Tax Act, XI of 1922, by the Commissioner of Income Tax. The matter arises out of an assessment of tax in the year 1933-34 on the income of the accounting year ending 31st March, 1933, of Messrs. P.C. Mullick and D.C. Aich who are the executors of the estate of Akshoy Kumar Ghose and are the assessees here.

The facts are set out in the Reference itself. Akshoy Kumar Ghose died in October 1931. Under his will Akshoy directed in paragraph 1:—

"After my death if I have any debts my said executors (executors) and trustees shall pay up the same out of the income of my property and on the occasion of my Addya Shradh they shall pay Rs. 10,000, ten thousand Rupees, out of the income of my property for expenses in connection with the Addya Shradh to the person who will be entitled to perform the Sradh."

In paragraph 2 he directed:—

"My said executors and trustees shall pay out of the income of my property, the costs of taking out probate of this last instrument of will and of (administration) of my property."

Question 1 asks :—

"Whether or not in computing the chargeable 'income' the whole of the amount (Rs. 10,000) provided in the will of Akshoy Kumar Ghose as payable out of 'income' on account of his 'sradh,' should have been left out of calculation, and not merely the actual amount paid in the year of assessment on account of the same (Rs. 5,537)?"

That is a question referred by the Commissioner at the instance of the trustees. The Commissioner himself has referred another question to us under Section 66 (*1*) and it is this :—

"Whether in computing the income chargeable to tax in this case, the Income Tax Officer should, on a proper application of the law, have excluded no part of the sum of Rs. 10,000?"

It is claimed by the excutors that no part of the Rs. 10,000 directed to be paid to the person entitled to perform the *sradh* is chargeable to income tax. The Commissioner has allowed, that is to say, exempted from taxation a sum of Rs. 5,537 which was the sum actually expended on the Addya Sradh of the deceased. The Addya Sradh ceremony is performed as a rule about one month after the death of the deceased. It is an act of piety and devotion on the part of the person who performs it. It may be, although personally I have some doubt, that expenses of the performance of this Addya Sradh, *i.e.*, the first *sradh* after the death of the testator, are part of the necessary funeral ceremonies contemplated by Section 316 of the Indian Succession Act. As I have said, I have some doubt whether it is one of the necessary funeral ceremonies, because it takes place some time after. If it is, then according to Section 316 of the Indian Succession Act it is the duty of an executor to provide funds for the performance of the necessary funeral ceremonies of the deceased in a manner suitable to his condition, if he has left property sufficient for the purpose. Section 320 of the Succession Act says :—

"Funeral expenses to a reasonable amount, according to the degree and quality of the deceased, and death-bed charges, including fees for medical attendance, and board and lodging for one month previous to his death, shall be paid before all debts."

If the expenses of Addya Sradh are part of the necessary funeral ceremonies of the deceased, then the expenses actually incurred, reasonable, proper and suitable to the condition in life of the deceased, would be payable by the executors, out of the general estate of the deceased. In this case however the deceased has been careful to direct his executors and trustees to pay Rs. 10,000 for the expenses is connection with the Addya Sradh to the person who would be entitled to perform the Sradh out of the income of his property. The testator seems to have been very careful and very anxious that no encroachment should be made on the corpus.

The case of *Trustees of The Sir Currimbhoy Ebrahim Baronetcy Trust* v. *Commissioner of Income Tax, Bombay*, is in point. The judgment of the Privy Council in that case was delivered by SIR SIDNEY ROWLATT and he reviewed the Indian Income Tax Act, 1922, and pointed out: " By Section 2 of that Act ' assessee ' is defined as meaning ' a person by whom income-tax is payable ' and ' person ' by virtue of the General Clauses Act, 1897, Section 3, sub-section 39, " includes any company or association or body of individuals, whether incorporated or not." Section 3, as amended, is as follows :—

" Where any Act of the Indian Legislature enacts that income-tax shall be charged for any year at any rate or rates applicable to the total income of an assessee, tax at that rate or those rates shall be charged for that year in accordance with, and subject to the provisions of, this Act in respect of all income, profits and gains of the previous year of every individual, Hindu undivided family, company, firm and other association of individuals."

In that case the trustees of the Baronetcy Trust were assessed. We are told that the income of the trust for the year 1928-29 consisted in part of interest from securities and in part of rents ; about 75 per cent. of it was paid to the Baronet, about 10 per cent. was carried to the two funds, and the remainder was absorbed by rates, taxes and other outgoings. It was held that the incorporated trustees were assessable under the Indian Income Tax Act, 1922, to income tax and super-tax for 1929-30 upon the whole income of the trust. In my view, in the same way, here the executors and trustees of the will of Akshoy

Kumar Ghose are assessable for the whole of their income notwithstanding that a portion of it was directed by the will to be paid to the person who would perform the Sradh ceremony; in other words, no deduction for the money directed to be spent on Sradh ceremony was allowable according to law. That answers question 1 and the supplementary question which the Commissioner of Income Tax has asked.

The second question is:

"Whether or not the cost of obtaining probate of the will of Akshoy Kumar Ghose should have been excluded from the chargeable 'income' of the assessees, particularly in view of the express provisions in the will that the same shall be payable out of the income?"

Here, again, the testator was careful about the *corpus* of the property and directed that the executors and trustees should pay out of the income of his property the cost of probate. According to Section 321 of the Succession Act, the expenses of obtaining probate or letters of administration, including the costs incurred for or in respect of any judicial proceedings that may be necessary for administering the estate, shall be paid next after funeral expenses and death-bed charges, so that the cost of probate normally will be payable out of the general funds of the estate. In my view no deduction should be allowed on the chargeable income in respect of the cost of obtaining probate of the will of Akshoy Kumar Ghose. The income of the trustees is, as I have pointed out when dealing with question 1, taxable and no deduction should be made for the costs of obtaining probate.

Before leaving this part of the case, I ought to deal with an argument put forward by Mr. Biswas in the case of *Raja Bejoy Singh Dudhuria* v. *Commissioner of Income tax, Bengal.* That was a case where the assessee claimed that he was not assessable on the whole of his normal income, because that income had been charged by the Court with a payment of a portion of it to his stepmother. Their Lordships of the Privy Council held that the assessee was only chargeable upon the balance of the income left after deducting the income which was payable to his stepmother. That case is different from this case. The difference is illustrated by a passage in the judgment of LORD MACMILLAN at page 200. It reads :—

"When the Act by Section 3 subjects to charge 'all income' of an individual, it is what reaches the individual as income which it is intended to charge. In the present case the decree of the Court by charging the appellant's whole resources with a specific payment to his step-mother has to that extent diverted his income from him and has directed it to his step-mother; to that extent what he receives for her is not his income. It is not a case of the application by the appellant of part of his income in a particular way; it is rather the allocation of a sum out of his revenue before it becomes income in his hands."

In the circumstances out of which questions 1 and 2 arise it is not the allocation of a sum out of the revenue before it becomes income in the hands of the trustees but it is a case of the application by the trustees under the directions of the testator of a part of the income in their hands in a particular way.

As regards question 3, it is as follows:—

"Whether or not the assessees were entitled to credit for the full amount of deductions of tax at source on account of securities and dividends, without any abatement in respect of the proportionate amount of charges allocated to and allowed against the total receipts from such sources?"

The Commissioner says:—

"This question is referred in accordance with the assessee's wishes, though it possibly is the result of some confusion in the mind of the assesseee regarding the facts involved in the assessment which are set out clearly below."

Mr. Biswas has dealt with the facts that underlie this question at some length. The question, however, is one of fact it may be a little involved, but nevertheless it is a question of fact and not one which ought to have been put to us. We, therefore, do not answer question 3.

The Income tax Department will have the costs of this Reference.

COSTELLO, J.—I agree in regard to the answers which have been given to the first question and to the second question which have been propounded for our consideration in the statement of the case made by the learned Commissioner of Income tax.

As regards the third question, the Commissioner himself has stated that that is referred in accordance with the assessee's

wishes, though it possibly is the result of some confusion in the mind of the assessees regarding the facts involved in the assessment. The learned Commissioner has set out the facts upon which the question is purported to be based and in paragraph 8 of his statement of the case he says :—

"The expression 'charges' used in paragraph 7 above is perhaps misleading and I should perhaps make it clear that out of the total income of the estate amounting to Rs. 1,56,701 income totalling Rs. 58,994 did not, under the provisions of the will, find its way to the executors for being dealt with as their income and accordingly they have not been made liable to tax therefor. This sum was utilised in some other manner in accordance with directions of the will and in so far as the assessment under dispute is concerned, it is no part thereof. Both the Income Tax Officer and Assistant Commissioner proceeded in the following manner: They treated this sum of Rs. 58,994 as no part of the income of the assessee at all. Thus from the total income of the Estate amounting to Rs. 1,56,701 they deducted this sum of Rs. 58,994 and found Rs. 97,707 to be the total income of the assessee from all the sources including agricultural sources and as the sum of Rs. 58,994 was not payable out of any particular source, it was reasonably treated as being drawn from all sources proportionately and thus the income of the assessee under the different heads was calculated as follows :"

and the Commissioner then has set out the manner in which the income was calculated.

It seems to me perfectly clear upon the facts stated by the learned Commissioner of Income tax that the assessees as regards this sum of Rs. 58,994 have no cause of complaint in connection with the assessment with which we are now concerned. It was not taken into account. If income tax has been deducted at source in respect of it, that is a matter which falls to be considered and dealt with, if necessary, under the relevant provisions of the Income tax Act for making a refund. Certainly it does not fall to be considered in connection with the assessment with which we are immediately concerned. I agree, therefore, that the learned Commissioner was correct in saying, as he said inferentially at any rate, that question 3 was not a matter which ought to have come before us at all.

With regard to the other two questions it is clear that Mr. Biswas appearing on behalf of the assessees had admitted that generally speaking executors are liable for income tax in respect of the income which finds its way into their hands in their capacity as executors and, were any authority needed for that proposition, it is only necessary to refer to the judgment of JENKINS, C.J., in the case of *A. H. Forbes* v. *The Secretary of State for India in Council*. In considering this matter, therefore, we may start with the basic proposition that *prima facie* the assessees are liable to pay tax on all the income of the testator which comes into their hands. Mr. Biswas sought to argue, however, as regards the first question that it was not only the sum of Rs. 5,537 that should be allowed as a deductible allowance but the whole of the sum of Rs. 10,000 which had been directed by the testator to be paid out of his income for expenses in connection with his Addya Shradh should have been deducted and treated as an allowance. As regards the second question Mr. Biswas also argued that the whole of the cost of obtaining probate of the will of the testator should have been excluded from the chargeable income of the assessees.

Mr. Biswas based his contention upon the principle underlying the decision in the case of *Raja Bejoy Singh Dudhuria* v. *Commissioner of Income tax, Calcutta*. The principle in that case appears to be this: If there is an allocation of a sum of money out of the revenue of an individual or, as in the present case as Mr. Biswas argued, out of the revenue of the executors, before that sum becomes "income" either in the hands of the individual or in the hands of the executors, then in that event the sum in question must be treated as being no part at all of the chargeable income of the assessees. In *Dudhuria's* case RANKIN, C. J., when the case was before this Court, with the concurrence of Mr. Justice C. C. GHOSE and Mr. Justice BUCKLAND dealt with the matter upon the footing that by the decree which this Court had made the Appellant's step-mother had a charge not only on the Appellant's zemindari property from which his agricultural income was derived but also on all his other sources of income including the assessable income. The learned Chief Justice rejected the suggestion that the Appellant's liability to his step-mother was of the same kind as his liability to provide for

his wives and daughter and he stated that the position was the same as if the appellant had received his various properties, securities and businesses under a bequest from his father upon the terms that these assets were charged with an annuity for the maintenance of the widow. The learned Chief Justice was of opinion that the case was not one of a charge created by the Raja for the payment of the debts which he had voluntarily incurred. In that view of the matter their Lordships of the Privy Council agreed and said that that was the correct approach to the question they had to determine. They then pointed out that SIR GEORGE RANKIN next examined the various exemptions and allowances conceded in Sections 7 to 12 of the several heads of income, profits and gains which were chargeable to income-tax under Section 6. They further pointed out that the learned Chief Justice had reached the conclusion that the appellant's liability to his step-mother did not fall within any of those exemptions or allowances. With that conclusion their Lordships of the Privy Council were in agreement. But as LORD MACMILLAN (at page 200 of report) states their Lordships did not agree with the learned Chief Justice in his rejection of the view that the sum paid by the appellant to his step-mother was not "income" of the appellant at all, and LORD MACMILLAN said, "This in their Lordships' opinion is the true view of the matter". It follows, therefore, that the *ratio decidendi* of *Dudhuria's* case was that the sum which the Raja had been ordered to pay to his step-mother was to be treated as not being part of the Raja's own income at all.

Mr. Biswas has invited us to come to the conclusion that both the sum of Rs. 10,000 directed in the will to be paid for the expenses of the *shradh* and the cost of obtaining probate of the will of Akshoy Kumar Ghosh ought to be regarded as never having been part of the income of the assessees at all and, therefore, outside the reach of the income tax authorities in connection with the assessment made upon the executors of Akshoy Kumar Ghosh. I agree with my Lord the Chief Justice in thinking that that is not a correct view of the matter. Normally, no doubt, executors under a will will be entitled under Section 316 of the Indian Succession Act (XXXIX of 1925) to expend such an amount as will be reasonably necessary for the performance of the funeral ceremonies of the deceased in a manner suitable to

his condition, provided of course he has left property sufficient for the purpose. In my view the Addya Shradh may not unreasonably be considered as an integral part of the necessary funeral ceremony of the deceased. Therefore apart altogether from the express provisions in the will, Akshoy Kumar Ghosh's executors would have been entitled to provide funds for the performance of that ceremony under the provisions of section 316 of the Indian Succession Act. The provisions in the Indian Succession Act are obviously based on the early English Common Law. They are attributable to the principles which have been laid down in various cases by the Courts in England. In connection with this particular point I should like to refer to the case of *Mullick* v. *Mullick* which was a case which went on appeal to the Privy Council from an order of the Supreme Court of Judicature at Fort William in Bengal in the year 1829. It is reported in 1 Knapp's Privy Council Reports, 245, and it is interesting to observe that LORD WYNFORD in the opening passage of the judgment given by the Judicial Committee of the Privy Council, said this:—

"The interest of Sovereigns, as well as their duty, will ever incline them to secure, as far as it is in their power, the happiness of those who live under their Government; and no person can be happy whose religious feelings are not respected. If this were a case between Europeans and Hindus, we would not take a step without the assistance of some of the persons from India, who are acquainted with the usages of that country with regard to the ceremonies that ought to be observed, and the works that ought to be performed on the death of an opulent native; for we should fear, lest by the judgment which we might advise his Majesty to pronounce, the feelings of the people of Hindustan might be wounded".

Then their Lordships went on to say:

"But this is a case where some members of a Hindu family object to the allowance that has been made to other members of the same family for the expenses of the obsequies of the father of all the litigant parties, and of the works which that father by his will directed to be done by those to whom he bequeathed his fortune. With respect to the obsequies, as the will gives no directions how they are to be performed, we have only to con-

sider upon the evidence which these parties have laid before us whether the sums allowed for their performance are more than have usually been expended at the funerals of persons of the same rank and fortune as the deceased. If they are more, as members of the family object to them, we ought not to sanction the expenditure".

Then his Lordship proceeded to consider whether or not the expenditure incurred ought to be allowed. That case indicates, as indeed does Section 316 itself, that apart from any provisions in the Will, it is the duty of the executors to provide funds for the performance of the necessary funeral ceremonies of the deceased. But those expenses in normal circumstances would have come out of the estate of the testator and they would be a charge on the corpus rather than on the income. In the present instance Akshoy Kumar Ghose gives definite and express direction that:—

"My said executors and trustees shall . . . on the occasion of my Addya Sradh pay Rs. 10,000 out of the income of my property for expenses in connection with the Addya Sradh to the person who will be entitled to perform the Sradh";

and (in the next paragraph),

"My said executors and trustees shall pay out of the income of my property, the costs of taking out probate of this last instrument of will and of administration of my property."

It seems to me—bearing in mind the observation of LORD MACMILLAN in the passage at the foot of page 200 in the report of the *Dudhuria* case—that this is a case of the allocation by the testator of a part of the income to be used in a particular way. It follows, therefore, that there was income coming into the hands of the executors, the present assessees, in such a manner that it became chargeable to tax before any part of that income was expended by the executors either for the purpose of discharging the costs of probate or for the purpose of providing expenses for the performance of the Addya Shradh ceremony of the deceased.

With regard to the first question, therefore, taking it in conjunction with the question which the learned Commissioner of Income-tax himself has referred under Section 66 (*1*), I would say that upon a proper construction of the Will the Income-tax

Officer ought not to have excluded any part of the sum of Rs. 10,000.

As regards the second question, I would say that the costs of obtaining probate of Akshoy Kumar Ghosh's will should not be excluded from the chargeable income of the assessees.

Reference answered accordingly.

[IN THE LAHORE HIGH COURT.]

COMMISSIONER OF INCOME TAX, PUNJAB

v.

HUKM CHAND JAGADHAR MAL.

ADDISON AND ABDUL RASHID, JJ.

January 24, 1936.

BAD DEBT—ASSESSEE OBTAINING DECREE AGAINST DEBTOR—APPEAL BY DEBTOR—CLAIM FOR DEDUCTION OF DEBT AS BAD DEBT AFTER DISMISSAL OF APPEAL—MAINTAINABILITY—DEBT, WHEN BECOMES BAD.

In the year 1924 the assessee instituted a suit upon a mortgage bond and obtained a mortgage decree in December, 1925. The mortgaged property was sold and for the balance remaining due the assessee obtained a personal decree against his debtor in 1928. Against this decree the debtor appealed and this appeal was dismissed in November, 1931. The assessee had been trying to execute the personal decree but did not realise anything. For the accounting year 1932-33 the assessee claimed deduction of the amount for which he had obtained a personal decree as a bad debt. The Income Tax Officer held that the debt had become bad in 1929. On appeal the Assistant Commissioner held that the debt had not become bad even in 1932-33. The Commissioner agreed with the Income Tax Officer. On a reference to the High Court: Held, *that there was no evidence whatever for coming to the finding that the debt had become bad in 1929; whether it became a bad debt in 1932-33 or later was a question of fact to be decided by the Income Tax authorities.*

Case stated by the Commissioner of Income Tax, Punjab and N.W.F.P. under Section 66 (3) of the Income Tax Act, as directed by the High Court by its order dated April 1, 1935. The facts of the case and the order of the High Court dated April 1, 1935, are reported at pp. 211 ff. of Vol. III of the *Income Tax Reports*: [Civil Ref. No. 67 of 1935].

J. N. Aggarwal, for the Commissioner.

Shamair Chand, for the Assessee.

ORDER.

On 1st April 1935 a Division Bench of this Court required the Commissioner of Income-tax to state a case and refer the following question for decision, namely:

'Whether there was any relevant and admissible evidence to support the conclusion that the sum of Rs. 26,721 became a bad debt in 1929.' The facts are stated in the order of the Bench and in the reference now made by the Commissioner. On 2nd December 1921, the asssessee obtained a mortgage deed in his favour from Sheikh Siraj Din for rupees 45,000 advanced as a loan. A suit was instituted in 1924 for the usual mortgage decree which was made on 19th December 1925. The property was sold and a balance of Rs. 26,721 remained due. A personal decree for the balance was obtained by the assessee against his debtor in 1928 and there was an appeal by the debtor to this Court against that decision. That appeal was not dismissed till 28th November 1931. In the meantime the assessee had been trying to execute the personal decree he had obtained, although the appeal against it was pending. In the assessment year 1933-34 he claimed the above amount as a bad debt, the accounting period being 1932-33. The Income-tax officer refused to grant him this relief on the ground that it had become a bad debt in 1929. The assessee appealed to the Assistant Commissioner who held that the debt had not yet become bad, as there was still time to proceed with the execution of the personal decree. The assessee went up to the Commissioner who upheld the original order of the Income-tax Officer that the debt had become bad in 1929. It is in these circumstances that the question arose.

On the record we have no hesitation in finding that there is no evidence of any kind that the debt became a bad debt in 1929. The appeal against the personal decree was still pending

and was not dismissed till the end of 1931. The assessee would have been guilty of a fraud if he had attempted to claim it as a bad debt earlier than the accounting year 1932-33. Whether it became a bad debt in that year or later remains a question of fact to be decided by the Income-tax authorities. With these remarks we answer the question referred in the negative. The assessee will have his costs from the Commissioner of Income-tax.

Reference answered accordingly.

[IN THE LAHORE HIGH COURT.]

SOM CHAND MALUK CHAND

v.

COMMISSIONER OF INCOME TAX, PUNJAB AND N. W. F. P.

SIR JAMES ADDISON AND ABDUL RASHID, JJ.

June 11, 1936.

BAD DEBT—ASSESSEE WHETHER BOUND TO CLAIM DEBT AS BAD DEBT WHEN DEBTOR GETS INTO DIFFICULTIES.

It does not follow that because a firm is in difficulties it will never recover and that all debts due by it should immediately be struck off as bad debts.

For the assessment year 1933-34 the assessee claimed that a sum of Rs. 776 should be deducted as bad debts. The Income Tax Officer disallowed it on the ground that the last balances were struck in 1930 and it had not been shown that the amount had become irrecoverable by the accounting year 1932-33. On appeal the Assistant Commissioner held that there was no hope of recovering the debts in 1930 when the last balances were struck and that the debts should have been claimed in 1930 to be bad debts. The Commissioner maintained the Assistant Commissioner's order. On an application by the assessee under Section 66 (3) of the Act the High Court held that the assessee was not bound to strike off the debts in 1930 merely because the debtor was in difficulties and the view of the Income-tax officer that it was too early to say that

the debt was a bad debt as only 2½ years had elapsed since th date of the last balance was understandable but the Commissioner's finding was not based on any evidence or sound reasoning, and directed the Commissioner to state the case.

Application under Section 66 (3) of the Indian Income Tax Act (XI of 1922) for an order directing the commissioner of Income Tax, Punjab and N. W. F. P. to state the case and make a reference to the High Court: [Civil Misc. Application No. 168 of 1936].

Prakash Chand, for the Assessee.

Jagannath Aggarwal, for the Commissioner.

ORDER.

SIR JAMES ADDISON, J.—The assessee Som Chand Maluk Chand was assessed for the assessment year 1933-34 to a certain sum. He claimed before the Income tax officer that the sum of Rs. 776 should not be included in the assessment as it consisted of bad debts. This was disallowed by the Income-tax officer on the ground that the last balances were struck in 1930 and that it had not been shown that the amount had become irrecoverable by the accounting year 1932-33. There was an appeal to the Assistant Commissioner who held that there was no hope of recovering the debts in 1930 when the last balances were struck and that the debts should have been claimed in 1930 to be bad debts. The matter was taken to the Commissioner, who happened to be the same Assistant Commissioner who had heard the appeal. He maintained his former order and the assessee has come to this court for a mandamus to issue on the Commissioner to state a case on this question.

In our judgment such a mandamus must issue. The debtor firm was in difficulties in 1930 but had acknowledged its debts, struck a balance and apparently at that time was ready to pay at the moment it could do so. It does not follow that because a firm is in difficulties it will never recover and that all debts due by it should immediately be struck off as bad debts. The view of the Income tax Officer is understandable that only 2½ years had elapsed since the date of the last balance and that it was too early to say that the debt was a bad debt. But it is difficult to follow the reasoning of the Assistant Commissioner or to find evidence on which he has come to his conclusion. Under the

provisions, therefore, of Section 66 (3) of the Income tax Act we require the Commissioner to state the case and refer the following question of law which arises :—

"Was there any evidence for the finding that the debts amounting to Rs. 776 became bad debts in 1930, and that this sum, therefore, could not be deducted in the assessment year 1933-1934 ?"

The assessee has also asked us to refer another question regarding the rate of interest fixed on a deposit of Rs. 1,11,500. As regards this, however, we are of opinion that the income tax authorities were justified in what they did and we, therefore, dismiss the application with respect to this question.

There will be no order as to costs.

Order accordingly.

[IN THE LAHORE HIGH COURT.]

DHANIRAM RAM GOPAL

v.

COMMISSIONER OF INCOME TAX, PUNJAB.

SIR JAMES ADDISON and ABDUL RASHID, JJ.

April 22, 1936.

REFERENCE—ORDER SETTING ASIDE FINDING THAT FIRM HAD DISCONTINUED—WHETHER PREJUDICIAL TO FIRM—RIGHT TO APPLY FOR REFERENCE—INDIAN INCOME TAX ACT (XI OF 1922), SEC. 66 (2).

The assessees had been assessed for several years as a Hindu undivided family and subsequently as a registered firm up to 1932-33. The Income Tax Officer held that the firm had divided and there had been discontinuance under Section 25 (2) of the Income Tax Act and that under Section 25 (3) no tax was payable. The Commissioner, in the exercise of his powers of revision under Section 33 of the Act set aside the order of the Income Tax Officer on the ground that discontinuance had not been established. The original assessees then moved for a reference under Section 66 (3): Held, *that the order passed by the Commissioner was not in any*

way prejudicial to the assessees as the persons to be assessed were their successors and not the assessees, and the assessees had therefore no right to apply for a reference.

Case stated under Section 66 (2) of the Indian Income Tax Act, 1922 by the Commissioner of Income Tax, Punjab & N.W. F.P. [Civil Reference No. 8 of 1936].

Mehr Chand Mahajan and *Kirparam Bajaj* for the assessees.

Jagannath Aggarwal, for the Commissioner.

ORDER

This is a reference under Section 66 (2) of the Income Tax Act regarding an order made by the Commissioner of Income Tax under Section 33 of the Act in the matter of the 1933-34 assessment of Messrs. Dhani Ram Ram Gopal. The assessee was assessed for several years as a Hindu undivided family and eventually as a registered firm on partition up to 1932-33. By order dated the 31st October 1933 the Income Tax Officer held that the firm had divided up and that there had been discontinuance under Section 25 (2) and that under Section 25 (3) no tax was payable.

On the 25th March 1935 this finding came before the commissioner who issued a notice of review before the expiry of 1934-35. An Advocate appeared before him and was heard. Thereafter he set aside the order of the Income Tax Officer, holding that discontinuance had not been established and he found accordingly for the purposes of this case, but he was careful to explain at various places in his order that in each of the new assessment cases, which would follow from this, the facts must be found by the Income-tax Officer independently, and that all that he was then doing was to clear out of the way of the Income Tax Officer the prior order in the original assessee's case as a matter of executive propriety, so that it might not stand to embarrass his findings in the cases of the other assessees.

The original assessee then moved the Commissioner for a reference to this Court and two questions have been referred.

"(1) Is an order under Section 33 setting aside a finding of discontinuance (contained in an order under Section 25 (2) without levy of tax and in the absence of refund claim under Section 25 (2)

and directing enquiry into succession in cases pending against the propounded successors, an order prejudicial to the predecessor assessee within the meaning of Section 66 (2)?

(2) If the answer to question No. (1) is in the affirmative was there any material on which the order in issue could be passed?"

The Commissioner has again been careful to point out in his order of reference that the actually assessed successors are the only persons aggrieved and that the findings as regards them will have to stand or fall on the evidence in their own cases and not on the evidence in this case. This seems to us to be undoubtedly correct, and as there was no enhancement of assessment, it also seems to us that the order passed on review by the Commissioner was not otherwise prejudicial to the original assessee, for the successors, if and when assessed, will have every right to be heard independently before the Income Tax authorities and to have a reference to this court on any question of law that may arise in their assessment. There has thus been no prejudice, and all that the learned counsel appearing for the original assessees was able to claim as prejudicial was the circumstance that the Income Tax Officer might feel himself compelled to follow the reasoning adopted by the Commissioner in his order in review. This, however, is not so, for the Commissioner has been careful to point out that there must be an independent assessment of the alleged successors who will be entitled to produce whatever evidence they can.

For the reasons given, we answer the first question in the negative, so that the second question does not require to be answered. This is a case in which we make no order as to costs.

Reference answered accordingly.

[IN THE LAHORE HIGH COURT.]

BADRI SHAH SOHAN LAL

v.

COMMISSIONER OF INCOME TAX, PUNJAB AND N. W. F. P. [No. 2].

SIR JAMES ADDISON AND ABDUL RASHID JJ.

June 10, 1936.

ACCOUNTS—BUSINESS SHOWING LARGER TURNOVER AND STOCK—PROFITS SHOWN ABNORMALLY LOW—FAILURE TO PRODUCE VOUCHERS OR MATERIAL TO SUPPORT ACCOUNTS—REJECTION OF ACCOUNTS—INDIAN INCOME TAX ACT (XI OF 1922), SEC. 13.

In the year 1931-32 *the business of the assessee (a bullion dealer) amounted to* 13 *lacs, in* 1932-33 *to* 18 *lacs and in* 1933-34 *to* 24 *lacs. In* 1931-32 *the gross profits were shown as* ·45 *per cent, in the year* 1932-33, *as* ·20 *per cent and in* 1933-34, ·19 *per cent. There was a steady rise in business and also in the stock but the profits showed a decline. The rate of profit shown was not even equivalent to the insurance payable on gold transmitted by the assessee. The assessee did not produce any vouchers or other material for checking his account books. The income tax authorities rejected his trading account and considering the profits made by others in bullion trade added a sum of Rs.* 6,000 *as additional profits, making the profits work out at* ·5 *per cent*: Held, *that in the circumstances of the case there was material to justify the action of the income tax authorities.*

Application under Section 66 (3) of the Indian Income Tax Act, 1922, for requiring the Commissioner of Income Tax, Punjab and N. W. F. P., to state a case and to make a reference to the High Court in the matter of the assessment of Messrs. Badri Shah Sohan Lal of Gujranwala for the year 1934-35. [Civil Mis. Application No. 81 of 1936].

Kirpa Ram Bajaj, for the assessees.

Jagannath Aggarwal, for the Commissioner.

ORDER.

This is an application under section 66 (3) of the Indian Income-Tax Act for the issue of a mandamus to compel the Income Tax Commissioner, Punjab, to state the case of Badri

Shah Sohan Lal, Saraf of Gujranwala to this Court. The question of law formulated on behalf of the assessee is as follows :—

'Is there any material on record justifying the rejection of the trading account of the petitioner and for adding the sum of Rs. 6,000 as alleged additional profits ?'

The assessee is the biggest bullion dealer in Gujranwala. In the year 1931-38 his business amounted to over 13 lacs of rupees, while the turnover in the year 1932-33 was over 18 lacs of rupees. The present application concerns the assessment for 1934-35 in respect of the accounting period ending on the 12th April 1934. The assessee's turnover was over 24 lacs of rupees. Though the business of the assessee has been rapidly increasing in the last 5 years, the percentage of the gross profit shown by him has been dwindling. In the year 1930-31, ·55 per cent were shown as the gross profits and, in the next year ·45. In the year 1932-33 the gross profits amounted to ·20 per cent and in the year under consideration to ·19 per cent. The Income Tax Officer was of the opinion that as the rate of profit disclosed by the assessee was below the average expectation of gold business during the year of its steady rise in price, the books of the assessee did not disclose the true state of his business. Keeping in view profits earned by other persons carrying on similar business, the Income Tax Officer added the sum of Rs. 6,000 to the income shown in the books. The assessee was consequently asked to pay income tax on a sum of Rs. 10,745.

The principal point urged by the learned counsel for the assessee was that as no flaw had been discovered by the income tax authorities in his trading account, the Income Tax Officer was not justified in adding an additional sum of Rs. 6,000 as estimated profits to Rs. 4,745 which were shown as actual profits in the trading account. The only question which the assessee is entitled to raise in this court is whether there was any material for making an addition of Rs. 6,000, on account of alleged profits, to the returned profits. The assessee's stock figure in 1932-33 was over 2 lacs and against this large capital, he only showed a gross profit of Rs. 3,747. In the year 1933-34, the stock rose to 2·9 lacs and the gross profits, therefore, were much less than secured interest payable on the best securities. As pointed out by the Commissioner the business requires considerable skill

and in spite of this the rate of profit shown was not even equivalent to the insurance payable on the gold transmitted by the assessee to Bombay.

The assessee did not produce any vouchers or any other materials which may enable a detailed check of his account books. The value of the account books produced by the assessee is, therefore, no higher than his mere word.

We, therefore, hold that there was material justifying the rejection of the trading account of the applicant and for adding the sum of Rs. 6,000 as additional profits. The rate of the profit works out at 5 per cent.

For the reasons given above we dismiss this application. Parties will bear their own costs.

Application dismissed.

[IN THE JUDICIAL COMMISSIONER'S COURT OF SIND.]

ZENAB KADERBHOY *v.* SECRETARY OF STATE.

RUPCHAND BILARAM and HAVELIWALA, A. J. Cs.

April 27, 1936.

REFUND—ASSESSMENT OF FIRM—RATE OF TAX APPLICABLE TO INDIVIDUAL PARTNERS LESS THAN RATE AT WHICH FIRM WAS ASSESSED—RIGHT TO APPLY FOR REFUND—DEATH OF PARTNER BEFORE ASSESSMENT OF FIRM—RIGHT OF HEIRS OF PARTNER TO APPLY FOR REFUND—INDIAN INCOME TAX ACT (XI OF 1922), SEC. 48 (2).

Section 48 (2) of the Indian Income Tax Act (which empowers a member of a registered firm to apply for a refund where the rate of income tax applicable to his total income of the previous year was less than the rate at which income-tax was levied on the profits of the firm) applies only to a person who has been assessed and does not apply to a person who was dead before the assessment on his income was made.

A person who was doing business in partnership with his sons died in December 1926 bequeathing his share in the profits of the firm to his widow. The sons carried on the business in the name of the old firm and in 1927 entered into a partnership among themselves and the firm was duly registered. The firm was taxed

for the assessment year 1927-28 on the profits of the year 1925-26 at the maximum rate of 18 pies in the rupee. The partners, i.e., the sons, applied under Section 48 and succeeded in getting a refund as the rate of tax on the individual income of each partner was less than the rate at which the firm's profits were assessed. The widow also applied for a refund :

Held, *that she was not entitled to a refund as her husband had died before the assessment had been made and she was not a partner of the firm at the time of the assessment. The fact that the profits had been bequeathed to her was not sufficient to entitle her to make a claim for refund as a partner.*

ZENAB BAI *v.* SECRETARY OF STATE FOR INDIA [1931] (22 S. L. R. 426) *affirmed.*

MITCHELL *v.* McNEILL & Co. [1927] (103 I. C. 120; 31 C. W. N. 630; A. I. R. 1927 Cal. 518; 2 I. T. C. 298) *referred to.*

First Appeal No. 13 of 1931, from a judgment of the Additional Judicial Commissioner of Sind.

Kimatrai Bhojraj, for the Appellant.
Partabrai D. Punwani, for the Crown.

JUDGMENT.

HAVELIWALA, A. J. C.—This is an appeal from the judgment of the learned Additional Judicial Commissioner of Sind who dismissed the appellant's suit with costs. Several issues were raised in the suit, but the learned Judge below tried the following two issues as preliminary issues: (1) Whether the suit as framed was competent? (2) Whether the plaintiff (appellant) had any claim to refund? On the first of these issues he held in the affirmative, and, on the second, in the negative.

The facts briefly are that the appellant Zenab Bai, widow of Kadirbhoy Karimji, filed a suit against the Secretary of State for India in Council for recovery of a sum of Rs. 120 being the amount of refund on account of income tax levied for the assessment year 1927-28. It appears that the appellant's husband Kadirbhoy Karimji along with his six sons, was doing business in timber at Karachi in the name of Kadirbhoy Karimji and he was a senior partner in the said firm. In December 1926, Kadirbhoy Karimji died and the partnership was dissolved. The deceased Kadirbhoy had bequeathed his share of profits in the firm to his

widow, the appellant. The sons, however, carried on business in the name of the old firm and in 1927 entered into a partnership between themselves. The partnership deed was duly registered. The firm was a registered firm and was taxed for the assessment year 1927-28 on the basis of the accounting year October 1925 to October 1926 at the maximum rate of 18 pies in the rupee. Each of the partners that is to say, the six sons of the deceased Kådirbhoy, applied under section 48 of the Income Tax Act for a refund of the tax, the rate of tax on the individual income of each partner being less than the rate at which the firm's profits were assessed. They were all paid the refund on their applications. The appellant also, on the strength of her husband's will, under which she was bequeathed the share of the firm's profits due to her husband applied to the Income tax authorities for a refund, but her application was refused on the ground that she was not a partner in the firm. The learned Additional Judicial Commissioner held that the plaintiff-appellant not being a partner in the firm could not make a claim for refund.

It was contended by Mr. Kimatrai on behalf of the appellant that though the firm was taxed for the assessment year 1927-28 on the footing of the profits of the accounting year 1925-26, the appellant should be deemed to be a partner in the firm inasmuch as the profits were bequeathed to her under the will of her husband and the firm being a registered firm she was entitled as partner to claim refund. Under Section 3 of the Act income tax is levied on the profits of a firm ; under Sec. 20, as it stood in 1928, assessment was to be made on the firm as constituted at the time the assessment was made. Section 48 (2) applies to the case of a member of a firm when the rate of income tax applicable to his total income is either less than the rate at which the firm's income is assessed or is below the minimum chargeable with income-tax; it applies to a person who has been assessed and does not apply to a person who was dead before the assessment on his income was made. The appellant's husband, Kadirbhoy, deceased, was not liable for assessment for the year 1927-28 because it was made in 1928, whereas he died in December 1926. It has been held in *Mitchell* v. *McNeill & Co.*, that a dead person cannot be assessed to income tax. Furthermore, the appellant was claiming the refund in the capacity of a partner in the firm, which she

was not. Kadirbhoy, having died in December 1926, ceased to be a member of the firm since that date. The deed of partnership of 1927 shows that the partnership was between the six sons only and the appellant has been not shown therein as a partner and in fact she was never a partner at all in the firm of Kadirbhoy for the year 1927-28. The fact that the profits were bequeathed to her under the will of her husband would not by itself entitle her to make any claim for refund as a partner. That being so, we are of opinion that the plaintiff-appellant could not claim refund as a partner though her husband Kadirbhoy who was a partner in the registered firm only until December 1926.

In view of this finding, it becomes unnecessary to discuss the other issue as to the jurisdiction of the Court to entertain the suit. Accordingly we dismiss the appeal with costs.

Appeal dismissed.

[IN THE CALCUTTA HIGH COURT.]

BENGAL COAL CO. LTD.

v.

JANARDAN KISHORE LAL SINGH DEO.

NASIM ALI AND EDGLEY, JJ.

March 24, 1936.

LESSOR AND LESSEE—LEASE OF COLLIERY—UNDERTAKING BY LESSEE TO PAY ALL TAXES UPON MINES—WHETHER INCLUDES INCOME TAX ON PROFITS OF MINE—NATURE OF INCOME TAX.

Where a lease deed relating to a colliery provided that " the lessee shall also pay and discharge all taxes, rates, assessments and imposition whatever being in the nature of public demand which shall from time to time be charged, assessed or imposed upon the said mines or any part thereof by the authority of Government of India or the said local Government . . . .", and in a suit against the lessee the lessor claimed that the lessee was bound to pay him the income tax which the lessor had to pay in respect of his income from the mines:

Held, *that income tax levied on the lessor in respect of the income of the mines cannot be said to be a tax charged or assessed upon the mines but was a charge on the lessor's total income and the lessor was not, therefore, entitled to claim the same from the lessee.*

Income tax is a tax on income and not on anything else. It is one tax, not a collection of taxes ; and it is also a personal tax.

LONDON COUNTY COUNCIL v. ATTORNEY-GENERAL [1901] (70 L.J.K.B. 77 ; 1901 A.C. 26) *referred to.*

Appeals from an appellate decree of the District Judge of Burdwan. [A. A. Nos. 856 and 1003 of 1933.]

S. C. Bose, S. K. Roy Chowdhury and *M. N. Das Gupta* for the Appellant.

S. N. Banerji, N. C. Bose, S. N. Mitra, and *Karunamoy Ghose* for the Respondents.

NASIM ALI, J.—These two appeals arise out of a suit for recovery of road cess, mine cess and income tax charged on the royalty payable for a certain colliery under the terms of a registered indenture of lease. The trial Judge decreed the suit. On appeal by the Defendants to the lower Appellate Court the learned District Judge has affirmed the decree of the trial Judge for road cess and mine cess but has dismissed the Plaintiffs' claim for income tax. Hence these two second appeals one (S.A. No. 856) by the defendants, and the other (S.A. No. 1003) by the Plaintiffs.

The point for determination in the two appeals is whether under the terms of the lease the Plaintiffs are entitled to recover (a) Road cess, (b) Mine cess, (c) Income tax, paid by them on the royalties reserved in the lease.

The relevant clauses in the lease are these:—

" (a)......................The lessee shall pay the royalties reserved in the lease at the time and manner appointed in that behalf and shall also pay and discharge all taxes, rates, assessments and imposition whatever, being in the nature of public demand which shall from time to time be charged, assessed or imposed upon the said mines or any part thereof by the authority of Government of India or the said local Government except demand of land revenue......".

It is contended on behalf of the lessee that the object of the covenant to pay taxes, rates, assessments and impositions was

not to throw upon the lessee the burden of the assessments payable by the lessor under the statutes, but only to state the liability of the lessee to pay his share of the assessment under the statute laws. The words "*all taxes, etc.,*" indicate that the lessee was made liable by the covenant for the whole of the impositions upon the demised mines payable by the lessor and the lessee and not simply for the portion payable by the lessee only. If the object of the covenant was to make the tenant liable for his share of the assessments only, there was no necessity for inserting it in the lease—because the liability was already fixed by the statutes. The covenant was not intended to be a mere surplusage but was framed with the object of throwing on the tenant the burden of obligations which, in the absence of such a covenant, might have fallen on the landlord.

The question is whether the burden of the obligations in the present case namely, road cess, mine cess and income tax which was on the plaintiffs has been thrown on the defendant by the operation of the covenants in the lease.

The contention on behalf of the tenant is that these impositions do not come within the covenants in the lease as they are not charged *upon the mines* but are charged *upon the landlord in respect of the mines.*

Now, what is the difference between an imposition *upon* the mines and an imposition *in respect of* the mines? All impositions are ultimately charged to the landlord or the tenant or both. Mr. Bose's contention however is that when parties to a covenant use the words "imposed, assessed or charged *upon* the premises" the meaning of the words is the *sense* in which the words are used in the statute. In support of his contention he invited our attention to the following passage in the judgment of BANKES, J. in *East Wood* v. *MacNab* [1914, 2 K.B. 361]:

"When parties to a covenant use the words 'charged on premises' the meaning of 'charged' *includes* the sense in which the word is used in the statutes."

In this passage the word "includes" has been used by the learned Judge. This word is wider than the word "means."

[With regard to road cess and mine cess his Lordship held that the obligations cannot be limited to charges on *the mines themselves* but extended to charges imposed in respect of them on persons,

namely landlord or tenant, and that the tenant undertook the liability to pay all charges of a recurring nature imposed by the statutes, whether they are described in the statute as imposed on the mines or on the lessor or the lessee in respect of them and that the decision of the Courts below on the point was right.]

As regards the claim for income tax, the contention of the lessor is that it is also within the convenant. For the purposes of the decision in the case I do not express any opinion on this question as the Plaintiffs' claim under this head fails for want of any materials to show what amount was imposed on them under the Income-tax Act for the demised mines only. The amount claimed by the Plaintiffs as income tax has not been *separately* assessed on them by the income tax authorities under the Income Tax Act. The amount claimed in the plaint has been laid at a certain figure by the Plaintiffs on calculation at a certain rate on their income from the mines. This rate is not the rate imposed on the Plaintiffs' income from mines alone by the income tax authorities. It has been fixed not only with reference to the income from the mines but also with reference to their other sources of income. The amount claimed under this head is not therefore the amount imposed by the income tax authorities under the Income Tax Act in respect of the mines only.

The result therefore is that both the appeals are dismissed. The parties are directed to bear their own costs in these two appeals.

EDGELY, J.—[His Lordship concluded as follows on the question of road-cess and mine-cess and then proceeded to deal with income tax.]

It seems to be clear, therefore, that the liability to pay the road cess and the Mines Board of Health cess arises directly in connection with the ownership of the mines or the receipt of income arising therefrom. These taxes are also separately assessed upon the persons concerned and they must I think be regarded as charges which the lessees have rendered themselves liable to pay under the terms of the covenant and I am of opinion that the lessors have clearly contracted themselves out of any statutory liability which they would otherwise have incurred with reference to these taxes.

Different considerations apply, however, in the case of income tax. With regard to this tax I am in agreement with the learned District Judge in thinking that it is a personal tax. Further, as was pointed out by Lord Macnaghten in the case of of the *London County Council* v. *The Attorney General*, income tax

"is a tax on income. It is not meant to be a tax on anything else. It is one tax, not a collection of taxes essentially distinct."

In this connection it is argued by learned Counsel for the Appellants in Appeal No. 1003 of 1933 that income tax must also be regarded as having been contemplated by the parties to the covenant, in view of the fact that mines are property and property is one of the heads of income chargeable to income tax under sec. 6 of the Income Tax Act (Act XI of 1922). It must however, be remembered that income tax is assessed under sec. 23 of the Act not separately in respect of the varions items mentioned in sec. 6, but upon the 'total income,' of the assessee. Under sec. 2 (15) of the Act the expression "total income" means the " total amount of income, profits, and gains from all sources to which this Act applies computed in the manner laid down in sec. 16," which latter section relates to exemptions and exclusions in determining the total income. Having regard to the provisions of the Income Tax Act with regard to assessment, it would in this particular case be impossible to separate any income tax which might be payable upon the mines from the total amount of income tax payable by the party concerned. The amount of the income tax payable by a person who owns mines or derives any portion of his income therefrom is not separately assessed upon the mines and the income arising therefrom but is assessed upon his total income which is determined according to certain specific directions contained in the Income Tax Act. In my view such a tax cannot be said to be a tax upon the mines and could not have been in contemplation of the parties when the lease was executed.

I therefore agree that these two appeals must be dismissed.

Appeal dismissed.

[IN THE ALLAHABAD HIGH COURT.]

CHAMBER OF COMMERCE, HAPUR

v.

COMMISSIONER OF INCOME TAX, UNITED PROVINCES.

BAJPAI AND COLLISTER, JJ.

April 6, 1936.

MUTUAL BENEFIT CONCERNS—CHAMBER OF COMMERCE REGISTERED AS COMPANY UNDER SEC. 26, COMPANIES ACT—INCOME PAID BY MEMBERS BY WAY OF ADMISSION FEES, SUBSCRIPTIONS, REGISTRATION FEES AND COMMISSION ON FORWARD CONTRACTS—LIABILITY TO INCOME TAX—NATURE OF SUCH INCOME—CHAMBER OF COMMERCE, WHETHER 'CHARITABLE INSTITUTION'—'CHARITABLE,' MEANING OF—REFERENCE—QUESTION FOUND IN ASSESSEE'S FAVOUR BY COMMISSIONER, WHETHER CAN BE RE-AGITATED IN HIGH COURT—INDIAN INCOME TAX ACT (XI OF 1922), SECS. 3, 4 (3), 6 (vi), 12—INDIAN COMPANIES ACT VII OF 1913), SEC. 26.

The assessee, the Chamber of Commerce, Hapur, was an association registered as a limited liability company under Section 26 of the Indian Companies Act. The object of the association was, among others, to promote and protect trade and commerce, to promote unity and friendliness among merchants and to facilitate transaction of business between merchants dealing in corn and persons entering into transactions with them. The members of the association were merchants of Hapur, some of whom were commission agents. Its income was derived from (i) admission fees and annual subscriptions of members, (ii) registraiion fees for grain-pits and commission on purchase and sale on forward delivery contracts entered into between members inter se *or between outsiders or between an outsider and a member. When an outsider was a party he had to register the contract through a member of the Chamber of Commerce. The income-tax authorities held that the income from admission fees and annual subscriptions was exempt from tax but assessed the company in respect of income from commissions and registration fees and also*

declined to make any allowance on account of expenses incurred in maintaining a hospital. On a reference by the Commissioner :

Held, (1) *that the assessee was not exempt from being assessed to income tax merely because it was an association registered as a company under Section 26 of the Companies Act (which provides for registration of associations not formed for earning profits) ;*

(2) *that the income from commission and registration fees paid by the members on their own account and on behalf of outsiders was not income derived from any source other than business and, as the Commissioner had found that such income was not income from business, it could not be differentiated from admission fees and subscriptions and was not liable to be taxed ;*

(3) *that the assessee was not a ' charitable institution ' within the meaning of the Income Tax Act and was not exempt from tax as such ;*

(4) *that the assessee was not entitled to claim exemption in respect of any money which it might have elected to spend on charity.*

Quaere : *Whether the Commissioner of Income Tax was right in holding that the income derived from commission on forward contracts and registration fees was not income from business.*

The High Court cannot resurrect a question which has been answered by the Commissioner himself in favour of the assessee.

Though an object may be of ' general public utility ' if the benefit goes to a section only of a community, every institution whose object is to benefit the public or a section of the public is not necessarily a charitable institution. Before an institution can be held to be ' charitable ' there must be an element of altruism, that is to say, the beneficiaries must not be able to claim the benefit.

BAORD OF REVENUE *v.* MYLAPORE HINDU PERMANENT FUND, LTD. (infra) *commented upon.*

LIVERPOOL CORN TRADE ASSOCIATION *v.* MONKS (infra) *distinguished.*

Cases referred to :—

BOARD OF REVENUE *v.* MYLAPORE HINDU PERMANENT FUND [1924] (I. L. R. 47 Mad. 1 ; 1 I. T. C. 217 ; 20 L. W. 27 ; 75 I.C. 833 ; A.I.R. 1923 Mad. 684).

COMMISSIONER OF INCOME TAX, BENGAL v. SHAW WALLACE & Co. [1932] (59 I.A. 206; I.L.R. 59 Cal. 1343; 1932 Comp. Cas. 276; 5 I.T.C. 211; 136 I.C. 742; A.I.R. 1932 P.C. 138).

COMMISSIONER OF INCOME TAX, BOMBAY v. MILLOWNERS' MUTUAL INSURANCE ASSOCIATION, LTD., [1932] (I.L.R. 56 Bom. 119; 33 Bom. L.R. 1581; 1932 Comp. Cas. 271; 135 I.C. 813).

LIVERPOOL CORN TRADE ASSOCIATION v. MONKS [1926] (2 K.B. 110; 95 L.J.K.B. 519; 134 L.T. 756; 42 T.L.R. 393; 10 Tax Cas. 442).

MELLODY, *In re* [1918] (1 Ch. 228; 87 L.J. Ch. 185; 181 L.T. 155; 34 T.L.R. 122).

NEW YORK LIFE INSURANCE CO. v. STYLES [1889] (14 App. Cas. 381; 59 L.J.Q.B. 291; 61 L.T. 201; 2 Tax. Cas. 460).

UNITED SERVICE CLUB, SIMLA v. CROWN [1921] (I.L.R. 2 Lah. 109; 61 I.C. 836; 1 I.T.C. 113; A.I.R. 1921 Lah. 208).

VERGE v. SOMERVILLE [1925] (1924 A.C. 496; 131 L.T. 107; 40 T.L.R. 279; 93 L.J.P.C. 173).

Case stated by the Commissioner of Income Tax, United Provinces under Sec. 66 (2) of the Indian Income Tax Act (Mis. Case No. 637 of 1934) in the matter of the assessment of the Chamber of Commerce, Hapur.

The facts are stated in the judgment.

S. K. Dar, K. C. Mital and *M. N. Agarwala* for the assessee.

K. Verma for the opposite party, Commissioner of Income-Tax.

JUDGMENT.

COLLISTER, J.—This is a case which has been stated by the Income Tax Commissioner under Section 66 (2) of the Indian Income Tax Act (XI of 1922). The assessee is the Chamber of Commerce at Hapur and the case relates to two assessment years, 1932-33 and 1933-34. The assessee is a company limited by guarantee which was registered in 1923 under Section 26 of the Indian Companies Act.

The objects for which the assessee was incorporated, as set forth in its Memorandum and Articles of Association, are as follows:—

(1) To promote and protect the trade, commerce and manufactures of India, and in particular the trade, commerce and manufactures of Hapur and district Meerut.

(2) To promote unity and friendliness amongst all merchants in general and dealers in grain in particular in respect of all subjects of common interest.

(3) To establish just and equitable principles in trade and to form a code or codes of practice to simplify and facilitate transaction of business between merchants dealing in grain, cotton seed, etc., at Hapur and elsewhere, and persons entering into those transactions with them.

(4) To maintain uniformity in rules, regulations and usages of trade.

(5) In case of mutual quarrels or dispute in business to settle them as between members of the association and between parties willing or agreeing to abide by the judgment and decision of the association.

(6) To consider all questions connected with trade, commerce, manufactures and affecting the rights and privileges of the whole mercantile community, specially dealers in grain and cotton etc., and to remove all difficulties in a lawful and constitutional manner.

(7) To acquire by purchase, taking on lease or otherwise lands and buildings and all other property, movable and immovable, which the association, for the purposes thereof, may from time to time think proper to acquire.

(8) To sell, improve, manage, develop, exchange, lease, mortgage or otherwise deal with all or any part of the property of the association, or the business of the association.

(9) To co-operate with other associations and Chambers similar to this association and to procure from and communicate to any such association such information as may be likely to forward the objects of the association.

(9*a*) To spend such sums of money as may from time to time be resolved upon by the Executive Committee or general body of the association on charitable and benevolent object or objects of public utility with the sanction of the latter.

(10) To do all such other things as may be conducive to the extension of trade, commerce or manufactures or

incidental to the attainment of the above objects or any of them.

Article (9*a*) did not originally occur in the momorandum; it was added in pursuance of a sanction to amend the Articles of Association which was obtained from the High Court on September 1, 1933. Application to that effect was made on the advice of the auditors, who had detected that the assessee was incurring without authority certain expenses in maintaining a hospital.

The income of the assessee is as follows:—

(1) Rs. 10 per month per member as admission fee.

(2) Re. 1 per member per annum as subscription.

(3) Re. 1 as registration fee for each *khatti* or gain-pit.

(4) 0-2-0 commission on every purchase and sale of 25 tons on forward delivery contracts.

The members of the assessee company are merchants of Hapur, some of whom are commission agents. It appears that the bulk of the income is derived from the commission which is paid on forward contracts. Any such contract may be entered into by two members *inter se* or it may be entered into by two outsiders or by an outsider and a member; but whenever an outsider is a party to the contract, he has to employ the services of a member of the assessee company who is a commission agent. Each contract is registered in the books of the assessee company, but it can only be registered in the name of a member and it is the member who has to pay the commission. He in his turn recovers it from the outsider or constituent, but so far as the company is concerned it is the member who is responsible for paying the commission.

The assessee objected that it was not liable to assessment under the Act; but the Income-tax Officer of Meerut overruled that objection and assessed the company to income-tax in respect to commission or registration fees, declining at the same time to make any allowance on account of the expenses incurred in maintaining a hospital. The admission fees and annual subscription only were held to be exempt. The assessee appealed on the following grounds:—

(1) That it was not an association working for profits and that no part of its income was liable to be distributed in the form of dividends or otherwise.

(2) That its income was derived from its own members in the form of contributions for its maintenance and was as such outside the scope of the Act.

(3) That it did not settle any profit or loss, but simply recorded the transactions and was not concerned with any payments.

(4) That it was incorporated under Section 26 of the Companies Act as an association limited by guarantee.

(5) That in any case the Income-tax Officer should have allowed the expenditure on charity.

The Assistant Commissioner of Income Tax dismissed the appeal, and thereupon the assessee moved the Commissioner of Income-tax to state a case and refer certain questions of law to this Court. The questions of law set out in their application were as follows :—

(1) Whether an association incorporated under Section 26 of the Indian Companies Act, as an association limited by guarantee not existing for earning profits, and prohibted under the law from dealing any dividends to its members, is liable to assessment, particularly in view of the fact that no relief under Section 43 of the Act is available to such an association, as in case of other associations not incorporated under Section 26 of the Indian Companies Act.

(2) Whether the income of the Chamber, derived from its members only in the shape of a certain fixed amount on each transaction registered in the Chamber, can be deemed to be " income, gains or profits " within the meaning of Section 4 of the Act, when such amount is to be spent not for distribution of any profits but for maintenance of its office and carrying out of objects enumerated in the memorandum of association.

(3) Whether the income of the Chamber of Commerce, Hapur, can be deemed to be " income of a religious or charitable institution derived from voluntary contributions or income derived from property held under trust or other legal obligation wholly for religious or charitable purposes " within the meaning of Section 4, Sub-section (3), Clauses (i) and (ii) and as such is exempt from assessment.

(4) Whether "income" of the Chamber is in any event derived trom " business " within the meaning of the Income Tax Act.

(5) Whether the expenditure on charity, in accordance with its memorandum of association, even prior to its amendment by the Honourable High Court, is liable to assessment.

The Income Tax Commissioner has, however, only referred questions Nos. 1 to 3 and No. 5 to this Court; he has not thought it necessary to refer question No. 4 because in his opinion the income of the assessee is not from "business" within the meaning of the Act, and he has accordingly conceded that point in favour of the assessee.

I will now proceed to deal with the questions which have been formulated by the Income Tax Commissioner.

Question No. 1.—There is no provision in the Act whereby an association incorporated under Section 26 of the Indian Companies Act is exempted as such from being assessed to income-tax. In fact, this was admitted before the Income-tax Officer. His assessment order dated March 22, 1934, shows that in the written arguments which were filed before him the following admission found place: "It may be conceded at the outset that the Chamber as such is not exempt from assessment as it is certainly a company registered under the Indian Companies Act and comes within the scope of Section 3 of the Income-tax Act."

I agree with the view of the Income-Tax Commissioner that there is no exemption in favour of such a company as such and that the non-applicability of Section 48 of the Act is an irrelevant consideration.

Question No. 2.—As I have already shown, the income of the assessee—apart from admission fees and subscriptions, which have been held to be exempt—is of two kinds; it consists (1) in payment of commission and registration fees which are made by members on their own account and (2) in payment of commission which, though made by members, actually comes from the pockets of outsiders. I will first deal with the former category.

Learned counsel for the assessee contends that the Chamber of Commerce at Hapur is a "mutual concern", *i.e.*, an association whose members contribute to a common fund for their mutual benefit and that the payments which are made by its members are on that account exempt from income-tax, being neither income, profits or gains within the meaning of the Act, they are contributions by individual members for a common

fund to be utilised by the aggregation of members for a common object. He relies on various authorities. The first case to which we are referred is from the House of Lords and dates back to 1889. It is the case of the *New York Life Insurance Company* v. *Styles*. It related to a Mutual Life Insurance Company which had no shares or shareholders, the members were the holders of participating policies, each of whom was entitled to a share of the assets and liable for all losses. A calculation was made by the company of the probable death-rate among the members and of the probable expenses and other liabilities, and the amount claimed for premiums from members was commensurate therewith. An account was annually taken and the greater part of the surplus of such premiums for expenditure referable to these polices was returned to the policy-holders as bonuses either by addition to the sums insured or in reduction of future premiums. The remainder of the surplus was carried forward as funds in hand to the credit of the general body of the members. It was conceded that the income derived by the company from investments and from all transactions with non-members was assessable to income-tax, but it was held by four out of six of the noble Lords who heard the appeal that no part of the premium income received under participating policies was liable to be assessed to income-tax as profits or gains under Schedule D. Schedule D in the Act of 1853 was concerned with

"any profits or gains arising to any person whatever from any profession, trade or vocation exercised in the United Kingdom."

The above view, namely, that no part of the premium income received under participating policies was liable to be assessed to income-tax was held by LORD WATSON, LORD BRAMWELL, LORD HERSCHELL and LORD MACNAGHTEN. LORD HALSBURY and LORD FITZ GERALD dissented from that view and were of opinion that the surplus returned or credited to members was liable to income-tax. Lord HALSBURY at the beginning of his address at page 389 stated: "I think the appellants do carry on a concern ....which brings in profit". LORD FITZ GERALD at page 404 stated:

"My Lords, we are now dealing with this case not as bet-

when the corporation and the individual policy-holders who may happen to be members in respect of their policies, but as between the Crown in respect of a public general tax and the corporation as a trading concern, which it is indubitably."

The majority, however, were of the opinion that the association was not a profit-making concern such as would attract income-tax.

In the case of *The United Service Club, Simla* v. *The Crown*, a learned single Judge of the Lahore High Court, relying on the case of *The New York Life Insurance Company* v. *Styles* held that the income of the United Service Club at Simla, a company registered under the Indian Companies Act, was not liable to be assessed to income-tax under the Indian Income Tax Act (Act VII of 1918) except to its house property. At page 110 (of 2 Lah.) the learned Judge observes:

"The money received by the Club from its members does not fall within Clause (iv) 'income derived from business' as the Club does not trade with its members, but the object for which it exists is their mutual benefit. If the money which the Club receives from its members were chargeable to income tax, it could only be so chargeable under Clause (vi) as 'income derived from other sources'. The question for determination is whether such money can be regarded as income at all."

He goes on to find that it is not income from other sources within the meaning of the Act. At page 113 he observes:

" . . . . I do not think that the money received by a club from the members composing it can be properly regarded as 'income', a word which itself seems to imply something received from outside."

It will be observed that Act VII of 1918 was then in force and in that Act the words "profits or gains", which find place in Section 4 (1) of Act XI of 1922, did not occur, but in *Commissioner of Income Tax, Bengal* v. *Shaw Wallace & Company*, their Lordships of the Privy Council held that the expansion of the language into "income, profits and gains" was more a matter of words than of substance.

In *The Commissioner of Income Tax, Bombay Presidency* v. *The Millowners' Mutual Insurance Association Limited* a Bench of the Bombay High Court held that in the case of a Mutual In-

surance Company limited by guarantee and formed by its members for the mutual insurance of members against liability to pay compensation to workmen employed by them and their dependents for accidents etc., the surplus of the cost or premiums and further sums received by the company from its members over its expenditure of the year was not liable to be assessed to income-tax as profits or gains of business under Sections 6 (iv) and 10 or any other section of the Indian Income Tax Act of 1922. There too the case of *The New York Life Insurance Company* v. *Styles* was relied upon. The learned Judges in discussing that case observed that the general principle therein laid down was that

"If a body of persons choose to contribute a sum of money for their own purposes, any surplus of that sum remaining after expenses have been paid cannot be regarded as profit."

In *Board of Revenue* v. *The Mylapore Hindu Permanent Fund Limited*, the capital of a mutual benefit society was made up solely of periodical investment by its members and the income of the society was mainly derived from interest earned on loans given solely to its members, every one of whom was by the rules eligible to take loans; and it was held by a special Bench of the Madras High Court that such interest earned by the society from its own members was not taxable "profits" within Section 9 of the Indian Income Tax Act (Act VII of 1918) in spite of the fact that the society was registered under the Indian Companies Act. In considering the case of *The New York Life Insurance Company* v. *Styles*, the learned Judges observed:

"The principle of that case is that income to be taxable must come in from outside and not from within."

The question does not seem to have been considered whether a mutual concern can trade with its members and whether the payment and receipt of interest on loans advanced might not amount to a money-lending business between the association and its members.

Learned counsel for the department on the other hand strongly relies on the English case of *Liverpool Corn Trade Association* v. *Monks*. In that case an association had been formed for promoting the interest of the corn trade and the objects

of the Association, as set out in the memorandum of association, were *inter alia* as follows—

(1) To promote or oppose legislative and other measures calculated to affect the corn trade generally, and for these purposes to petition Parliament and take such other steps and proceedings as may be expedient, and to define, make and maintain uniformity and expediency in the rules, regulations, usages and customs of the said trade, and to establish just and equitable principles therein.

(2) To adjust and settle disputes between persons engaged in the said trade by establishing a tribunal of reference for the amicable adjustments of such disputes.

(3) To provide, regulate and maintain a suitable building exchange, market and room for the purposes of the corn trade in Liverpool.

(4) To establish and maintain a clearing house for the clearance of contracts or periodical settlement of contracts, and for facilitating payments between persons engaged in the corn trade.

In order that the facts of that case may be understood I quote the following observation from the beginning of the judgment, which was delivered by ROWLATT, J.: "In this case there was a company with a share capital of £ 60,000 in 400 shares of the unusually large denomination of £ 150 each, and its object was to maintain, and it did maintain, buildings for the purposes of the corn trade in Liverpool, and afford a number of facilities in those buildings. It made charges to its members and to other people proportionate to the use they made of the facilities; and it could, and at one time it did, declare a dividend upon its share capital. The major part of the clientele of the company, or at any rate the more important part, were, I have no doubt, the members themselves, and I suppose the members joined in order that, as members, they might have the benefit of the facilities upon more reasonable terms than outsiders. They paid an entrance fee when they became members. There is nothing more to be said, I think, about the company, except perhaps this, that a member had to become a shareholder, but that he could not hold more than two shares, and if he had more than one, the extra one might be requisitioned in order to enable a new entrant to obtain his share if he could not acquire a share otherwise.

"The question here is whether the profit which the company makes out of what the members pay to it, is taxable income of the business which the company undoubtedly carries on. The alleged profit consists of the amount by which the entrance fees of the members and their subscriptions for the various facilities exceed the cost of keeping up the buildings and affording the facilities. I do not see why that amount is not a profit. The company has a capital upon which dividends may be earned, and the company has assets which can be used for the purpose of obtaining payments from its members for the advantages of such use, and one is tempted to ask why a profit is not so made exactly on the same footing as a profit is made by a railway company who issues a travelling ticket at a price to one of its shareholders, or at any rate as much a profit as a profit made by a company from a dealing with its own shareholders in a line of business which is restricted to the shareholders. If there were a railway company which only carried its shareholders, one would say that when it afforded the advantage to a shareholder of performing an act of transit for him, being paid by the shareholder therefor, that the profit thereby made was a profit of the company just as much as if the shareholder was a stranger."

That case is of course distinguishable from the cases of *The New York Life Insurance Company* v. *Styles* and from the case with which we are now dealing by the fact that there was a share capital and that there were shareholders who had a right to demand dividends, if declared. At the same time it is to be observed that notice was taken of the fact that the company dealt with persons who happened to be the owners of the share capital "affording benefits to those persons individually for which they pay money by way of subscriptions and by way of entrance fees" and the learned Judge accepted the Attorney-General's contention that there was no reason at all for regarding otherwise than as profits the difference which was obtained by dealings between the corporation and the persons who happened to be its members.

It is I think settled—and in fact it is not disputed—that in certain cases at least money paid in by members of a "mutual concern" is exempt from income tax; and the fact that the Chamber of Commerce at Hapur is in one aspect at least a

mutual concern seems to have been recognized by the income-tax authorities, inasmuch as they have conceded that the admission fees and subscriptions are contributions by members such as did not attract income tax. At the same time learned counsel for the assessee concedes that a "mutual concern" may trade with its members and that in such circumstances the profits earned thereby will be liable to tax. The Income Tax Commissioner, however, has clearly conceded in his statement of the case that the income from commission and registration fees is not income from "business" within the meaning of Section 6 (iv) of the Act; but he is of opinion that it is taxable on the ground that it is "payments made by members for services rendered to them by the assessee." I refrain from expressing any view as to whether the Income Tax Commissioner was right in conceding that these payments are not income from business, for I am clearly of opinion that the department is bound by that admission. This Court is only called upon to answer the questions of law which have been formulated by the Income Tax Commissioner in his statement of the case. It is true that the Income Tax Officer and the Assistant Commissioner of Income Tax both held that these payments were income from "business" and on that account the assessee asked the Income Tax Commissioner to refer this question to the High Court; but I do not think that this Court can resurrect a question which has been answered by the Commissioner himself in favour of the assessee. Now, if these payments are not income from business, it is difficult to see from what "other source" a mutual concern can derive profits. Since it has been held by the Income Tax Authorities that these payments are not income from business, I find myself unable to differentiate between them and the admission fees and subscriptions which have been held to be contributions other than "income" and therefore not taxable.

As regards payments which are made by outsiders through members, learned counsel for the assessee argues that there is no privity between the company and the outsiders and that these payments must therefore be deemed to be payments made by members in the same way as those which are made by members on their own behalf. We are not impressed by this argument. That the Association has direct dealings with outsiders is shown

in Paragraph 5 of the objects of the Association as set forth in the memorandum and also by Rule 7 of Appendix B as reproduced on page 15 of the paper book. At the same time it seems to me that such payments cannot appropriately fall under any head other than "business" and since it has been conceded—whether rightly or wrongly—by the Income Tax Commissioner that they are not income from "business" I must hold that they are not taxable as income from "other sources" within the meaning of Section 6 (vi) of the Act. For reasons already given I express no opinion as to whether they do in fact fall under the head of "business".

Question No. 3—Learned counsel for the assessee admits that Clause (*i*) of Sub-section (3) of Section 4 of the Act has no application. There remains Clause (*ii*) of that sub-section which provides that "any income of a religious or charitable institution derived from voluntary contributions and applicable solely to religious or charitable purposes" is exempt from income tax. "Charitable institution" is not defined, but "charitable purpose" is defined as including "relief of the poor, education, medical relief and the advancement of any other object of general public utility." Obviously the word "charitable" in the Act has a technical significaance other than the meaning which it bears in common parlance. The ostensible object of this association is to provide facilities of trade and to improve business. As regards the question of "general public utility", it has been held in numerous cases that the requirements of the law will be satisfied if the benefit goes to a section of the community—*vide*, for instance, the English case of *In re Mellody*. In that case a testatrix bequeathed the income of a fund in trust to provide an annual treat or field day for the school children of a certain locality, or as many of such children as the same would provide for; and it was held that the be quest was a good charitable gift. At the same time every institution whose object is to benefit the public or a section of the public is not necessarily "charitable". In the Privy Council case of *Verge* v. *Somerville and others* LORD WRENBURY in considering whether a valid charitable trust had been created, made the following observation :—

"To ascertain whether a gift constitutes a valid charitable trust . . . . . a first inquiry must be whether it is public—

whether it is for the benefit of the community or of an appreciably important class of the community. The inhabitants of a parish or town, or any particular class of such inhabitants, may, for instance, be the objects of such a gift, but private individuals, or a fluctuating body of private individuals, cannot.

In the present case the persons who are actually benefited are (1) those particular individuals who are members of the association and (2) such outside merchants as may elect, when doing business at Hapur, to do it through the Chamber of Commerce. I feel some doubt as to whether in the circumstances an object of general public utility as contemplated by the Act is being advanced by the assessee. Further, it seems to me that before an institution can be held to be "charitable" there must be an element of altruism; that is to say, the beneficiaries must not be able to *claim* the benefit. That condition is wanting in the present case. Moreover, the contention of learned counsel for the assessee that there is no privity between the assessee and outsiders and that this is a "mutual concern" of the members who compose the association appears to me to be inconsistent with his claim that the assessee is a "charitable institution" within the meaning of Clause (*ii*) of Sub-section (3) of Section 4 of the Act. The whole idea of a "mutual concern" is that the particular members composing it should be benefited.

Without considering whether the other requirements of Clause (*ii*) are or are not satisfied, I am of opinion that for the reasons given above the assessee is not a "charitable institution" within the meaning of the Act and is not as such exempt from tax.

Question No. 5—Learned counsel for the assessee concedes that apart from other considerations, the assessee cannot claim exemption *quoad* any money it may have elected to spend on charity.

BAJPAI, J.—I agree.

BY THE COURT—Our reply to the reference is as follows :—

Question No. 1. This question is answered in the affirmative.

Question No. 2.—The answer to this question is that such payments are not income from any sources other than business. We express no opinion as to whether the Income Tax Commis-

sioner's admission that they are not income from business is or is not correct.

Question No. 3. The answer to this question is in the negative.

Question No. 5. The answer to this question is in the affirmative.

The assessee will receive his costs of this reference from the department. He is entitled to recover counsel's fee according to the certificate filed by Mr. Dar.

The hearing of this case occupied four days and it was argued with ability by Mr. Kamla Kant Verma on behalf of the department. He should file his certificate within six weeks.

Let a copy of this judgment be sent to the Commissioner of Income Tax.

Reference answered accordingly.

[IN THE ALLAHABAD HIGH COURT.]

MOHAMMAD ASLAM
v.
COMMISSIONER OF INCOME TAX, UNITED PROVINCES.

COLLISTER AND BAJPAI, JJ.

August 7, 1936.

ASSOCIATION OF INDIVIDUALS—CO-OWNERS HAVING SPECIFIED BUT UNDIVIDED SHARE IN PROPERTY—WHETHER TAXABLE AS 'ASSOCIATION OF INDIVIDUALS'—MEANING OF 'ASSOCIATION OF INDIVIDUALS'—APPOINTMENT OF COMMON COLLECTING AGENT, EFFECT OF—INDIAN INCOME TAX ACT (XI OF 1922), SEC. 3.

The expression 'association of individuals' in Section 3 of the Indian Income Tax Act is ejusdem generis *with the word immediately preceding,* viz., *'firm' and before there can be an association of individuals within the meaning of the section it must first be shown that the association has at least some of the attributes of a firm or partnership though not in the strictly legal sense of the term.*

Persons having specified but undivided shares in property which produces income do not come within the expression association of individuals in Section 3 of the Act and are not liable to be assessed to income-tax as such. Even the appointment by a body of co-owners of a common collecting agent will not convert such body of co-owners into an association of individuals within the meaning of Section 3.

A mandi *consisting of some shops, houses and a piece of open ground on which a market was held originally belonged to one person who died in 1860. In 1925, 26 persons had become owners of the* mandi *by right of association or transfer. Up to 1925 the owners used to lease the* mandi *to* thekadars, *but in that year they appointed an agent to collect rents and maintain accounts :* Held, *that the owners of the* mandi *did not constitute an association of individuals within Section 3 of the Income Tax Act and were not liable to be assessed to income-tax as an association.*

Cases referred to:

COMMISSIONER OF INCOME TAX, MADRAS v. MOHIDEEN SAHIB OF BELLARY [1927] (2 I.T.C. 472 ; 53 M.L.J. 719 ; 26 M.L.W. 655 ; 106 I.C. 226 ; A.I.R. 1917 Mad. 1052).

COMMISSIONER OF INCOME TAX, MADRAS v. MRS. J. V. SALDHANA [1932] (I.L.R. 55 Mad. 891 ; 62 M.L.J. 600 ; 35 M.L.W. 735 ; 138 I.C. 1 ; A.I.R. 1932 Mad. 373).

ELIAS, *In re* [1935] (1935 I.T.R. 408 ; 40 C.W.N. 476).

HOTZ TRUST OF SIMLA v. COMMISSIONER OF INCOME TAX [1930] (I.L.R. 11 Lah. 724 ; 5 I.T.C. 8 ; A.I.R. 1930 Lah. 929).

MIAN CHANNU FACTORIES UNION v. COMMISSIONER OF INCOME TAX [1936] (1936 I.T.R. 203 ; A.I.R. 1936 Lah. 548).

TRIBUNE PRESS, TRUSTEES OF v. COMMISSIONER OF INCOME TAX [1935] (1935 I.T.R. 246 ; I.L.R. 16 Lah. 829 ; 158 I.C. 306 ; A.I.R. 1935 Lah. 570).

Case stated by the Commissioner of Income Tax on his own motion under Section 66 (1) of the Indian Income Tax Act (XI of 1922) [Mis. Case No. 335 of 1934].

M. N. Kaul (for *K. N. Katju*) and *P. L. Banerji* for the assessees.

K. Verma for the Commissioner of Income Tax.

JUDGMENT.

COLLISTER, J.—The Commissioner of Income Tax has on

his motion under Section 66 (1) of the Income Tax Act referred the following two questions to this Court for decision: —

"(1) Whether on the facts of the case stated below (*i.e.*, in his statement of the case) the various co-sharers owning the Mandi known as the Khalifa Mandi at Allahabad constitute an association of individuals within the meaning of Section 3 of the Income Tax Act ?

(2) If the answer to the above question be in the affirmative, whether in view of the fact that Mufti Mohammad Aslam has, subsequently to the issue and service of the notice under Section 2 (12) of the Income Tax Act, 1922, transferred his proprietary interest to his wife, the Income Tax Officer is debarred from treating him as the principal officer of the association within the meaning of the section quoted above ?"

The Khalifa Mandi consists in some shops, houses and a piece of open ground on which a market is held. It originally belonged to one Mufti Karim Quli who died in 1860. It appears that from 1925 onwards twenty-six persons have by right of association or transfer been the owners of this Mandi. Up to 1925 the owners used to lease the Mandi *thekadars*, but in that year they appointed a man named Kanhaiya Lal to collect rents and maintain accounts. These accounts were kept in Hindi ; but subsequently, for the convenience of some of the co-sharers, another man, named Abdul Shakoor, was also appointed, who wrote in Urdu. It appears that Kanhaiya Lal has now resigned, but we do not know the date of his resignation and we do not know whether Abdul Shakoor is still in the employment of the owners.

As regards question No. (1) the learned counsel for the department contends that an association of individuals within the meaning of Section 3 of the Income Tax Act will cover any case where a number of persons have a specified but undivided share in property which produces income ; but he has not been able to show us any authority for this definition. Taken by itself, it cannot be denied that the expression is capable of a very wide interpretation, but having in view its context and the Act as a whole, we do not think it was the intention of the Legislature that the words should have so comprehensive a meaning. Originally the words used in the Act were "individual, company

firm and Hindu undivided family", but under an Amending Act of 1924 (II of 1924) the words "individual, Hindu undivided family, company, firm and other association of individuals" were substituted. There is no comma after the word "firm" and from this as well as from the fact that the words "Hindu undivided family" have been transposed to a higher position in the sentence it must be inferred that it was the intention of the Legislature that the expression "other association of individuals" should be *ejusdem generis* with the word immediately preceding, *i.e.*, the word "firm". Thus, before there can be an association of individuls within the meaning of the section, it must first be shown that the association has at least some of the attributes of a firm or partnership, though not in the strictly legal sense of the term. Learned counsel for the department has referred us to the following cases: *Commissioner of Income tax, Madras* v. *Mohideen Sahib of Bellary*; *Hotz Trust of Simla* v. *Commissioner of Income Tax; Commissioner of Income Tax, Madras* v. *Mrs. J.V. Saldhana*; *Trustees of the Tribune Press* v. *Commissioner of Income Tax*; *In the matter of Messrs. B. N. Elias* and *Mian Channu Factories Union* v. *Commissioner of Income Tax, Punjab.* None of the above cases, with the possible exception of *B. N. Elias, In re,* is of much assistance to us in deciding the questions which are laid before us. In the last mentioned case it was held that persons who have joined themselves together in the purchase of a property and have remained joined as owners and for holding and using it in order to make gain thereby are an association of individuals within the meaning of Section 3 of the Income tax Act. The following observations of the learned Chief Justice in that case may with advantage be quoted:

"Those words 'association of individuals' have to be construed in their plain, ordinary meaning. There is no difficulty about the word 'individuals'. Associate means, according to the Oxford Dictionary, 'to join in common purpose, or to join in an action.' Did these individuals join in a common purpose, or common action, thereby becoming an 'association of individuals'? In my view, they did. In the first place, they joined together in the purchase of this property on January 9, 1920. In the second place, they have remained joined as owners of

this property from the date of the purchase down to the present time. Thirdly, they have joined together, as the powers-of-attorney show, for the purpose of holding this property and of using it for the purpose of earning income to the best advantage of them all."

We now have to see what are the facts in the present case. The Commissioner of Income tax at one place states that in 1925

"the owners as a body employed one Kanhaiya Lal, an accountant and a servant of the former lessees, to collect rents and maintain the account thereof.

He then mentions that subsequently a second man was employed and he then goes on to state:

"The collections were made generally by the staff; but sometimes the cosharers made them themselves and reported them to the accountant for the purpose of writing up and adjusting the accounts."

It thus appears that the rents were sometimes collected by one or other of the accountants and sometimes by individual cosharers. Thus, although the learned Commissioner has stated at the beginning that these accountants were appointed by the owners as a body, it seems at least doubtful whether all the cosharers had consented or were satisfied with their appointment. It also appears that there is no large measure of agreement among the cosharers. It does not appear from the Commissioner's statement of the case that the accountants had authority to do anything more than collect rents and maintain accounts. On page 4 of our printed book we read that

"suits have been filed by some of the cosharers for the recovery of rent in respect of their shares only."

Even if the accountants were acting under the authority of all the cosharers, we do not think the mere appointment by a body of co-owners of a common collecting agent will convert such body of co-owners into an "association of individuals" within the meaning of Section 3 of the Act. We express no opinion as to what the position would be if the co-owners of an income producing property appointed one or more persons, whether from among themselves or from outside, to perform all the functions of a common scheme of management. For the reasons given

we are unable to agree with the Income Tax Commissioner that the owners of the Khalifa Mandi are an "association of individuals" within the meaning of Section 3 of the Income Tax Act. This is our reply to question No. (1) of the reference.

In this view of the first question, the second question does not fall to be decided.

The assessee will be entitled to his costs from the department. Mr. Kamla Kant Verma on behalf of the department should file his certificate within two months. The hearing of this case occupied a whole day.

Reference answered accordingly.

[IN THE BOMBAY HIGH COURT.]

COMMISSIONER OF INCOME TAX, BOMBAY

v.

GOPAL VAIJNATH MANOHAR.

BEAUMONT, C. J., AND RANGNEKAR, J.

March 11, 1936.

REFERENCE—COSTS—ORDER DIRECTING COMMISSIONER TO PAY ASSESSEE'S COSTS—ASSESSEE'S RIGHT TO RETURN OF DEPOSIT OF RS. 100—INDIAN INCOME TAX ACT (XI OF 1922), SEC. 66 (2).

The fee of rupees one hundred which an assessee who applies for a reference under Section 66 (2) of the Indian Income Tax Act has to pay forms part of the assessee's costs of the reference and consequently an order of the High Court in a reference directing the Commissioner to pay the costs of the assessee covers the return of the fee as being part of the costs of the assessee.

In cases in which the assessee is ordered to pay costs, the Court can if it considers that credit should be given to the assessee for the fee, give the Commissioner his costs less the rupees one hundred.

The Court has no jurisdiction to order the fee as such to be refunded ; it can only deal with the matter in relation to costs.

Commissioners of Income Tax, Burma v. J. I. Milne [1934] (1934 I.T.R. 25; I.L.R. 11 Rang. 454; 148 I.C. 98; A.I.R. 1934 Rang. 4) *followed.*

Civil Application No. 1161 of 1935 from an order of the High Court of Bombay on its Original Side in Civil Reference No. 2 of 1935.

K. Mc. I. Kemp and *A. P. Lille* for the Commissioner.

K. S. Shavaksha, Ranchoddas and *Hakim* for the assessee.

Beaumont, C.J.—This application raises a short point of practice in connexion with references under Section 66 of the Income Tax Act. That section provides under sub-s. (2) that in certain circumstances the assessee may by application, accompanied by a fee of Rs. 100 or such lesser sum as may be prescribed, require the Commissioner to refer to the High Court any question of law. Then there is a proviso to the section, which specifies the cases in which the Rs. 100 fee can be recovered. The proviso directs that if the Commissioner rejects the application on the ground that it is time-barred or otherwise incompetent, or if in exercise of his powers under sub-s. (3), the Commissioner refuses to state a case, or if the Commissioner decides the case under Section 33 in revision, the assessee may, within 30 days from the date on which he receives notice of the order passed by the Commissioner, withdraw his application, and if he did so, the fee of Rs. 100 shall be refunded. Those are the only cases in which the fee is directed to be refunded. Then sub-s. (6) provides that where a reference is made to the High Court on the application of an assessee, costs are to be in the discretion of the Court.

Now in this case a reference was made to the Court, and the Court made an order that the Commissioner should pay the costs on the original side scale, that being the usual order made in cases in which the assessee is successful. The assessee has included in his bill of costs the fee of Rs. 100 paid under Section 66 (2), and the Taxing Master has allowed it, and the question on this application is whether the Taxing Master was right in so doing. Dealing with the matter in the first instance under the Act and apart from authority, the position is that this fee is to be paid as a preliminary to starting the proceedings for a reference. The Commissioner cannot be put in motion to refer a point of law to

the High Court until the fee has been paid, though no doubt the fee is paid before the reference is actually made. The fact that the section, whilst providing for the return of the fee in the event of the reference not being effective, makes no provision for the return of the fee if the reference is effective and the decision of the Court goes against the Commissioner, seems to suggest that the legislature intended that where the reference comes before the Court the question of return of the fee should be in the discretion of the Court as part of the costs of the reference, and as the payment of the fee is a necessary incident to the obtaining of a reference, it seems to me that under the Act it is legitimate to hold that this fee is part of the assessee's costs of the reference.

We are told that it has not been the practice up to now to allow the fee, but, on the other hand, it is the practice to allow the fee in other High Courts. We have been referred particularly to a recent decision of the Rangoon High Court, *Commissioner of Income Tax, Burma* v. *J. I. Milne*, where the learned Chief Justice, although he rather indicates the view that if the matter had been free from authority he would have been disposed to hold that this fee was not part of the costs of the reference, nevertheless followed the practice of the High Courts of Madras, Allahabad, Patna and Lahore, and directed the fee to be treated as part of the assessee's costs. The Advocate-General says that in some of the decisions of the other High Courts the fee has not been treated as part of the costs, but the Court has made an order that it be refunded. In my view the Court has no jurisdiction to order the fee as such to be refunded; it can only deal with the matter in relation to costs. In my opinion, the fee is part of the assessee's costs of the reference, and consequently our order directing the Commissioner to pay the costs covers the return of the fee as being part of the out-of-pocket expenses of the assessee. In cases in which the assessee is ordered to pay costs, the Court can, if it considers that credit should be given to the assessee for the fee, give the Commissioner his costs less Rs. 100. Application is dismissed with costs on the original side scale.

RANGNEKAR, J.—I agree.

Application dismissed.

[IN THE BOMBAY HIGH COURT.]

SARUPCHAND

v.

COMMISSIONER OF INCOME TAX, BOMBAY.

BEAUMONT, C.J., and RANGNEKAR, J.

March 11, 1936.

ACCOUNTING—CHANGE OF METHOD OF ACCOUNTING REGULARLY EMPLOYED BY ASSESSEE—PERMISSIBILITY—REFERENCE—QUESTION WHETHER METHOD OF ACCOUNTING HAS BEEN CHANGED—QUESTION OF FACT—INDIAN INCOME TAX ACT (XI OF 1922), SECS. 13, 66.

An assessee is entitled to change the method of accounting regularly employed by him. What he must alter, however, is his regular method, that is to say, he must abandon what up to that time, has been his regular method, and start a new regular method, and not merely a new method for a casual period.

The question whether the regular method of accounting has been changed is a pure question of fact upon which the Commissioner cannot be directed to state a case; but if the regular method has been changed in fact the Commissioner is bound to recognise the changed method.

Applications (Nos. 1074 and 1075 of 1935) under Sec. 66 (3) of the Indian Income Tax Act for an order requiring the Commissioner of Income Tax, Bombay, to state a question of law to the High Court.

G. C. O'Gorman and *Y.V. Dixit* for Assessee.

K. McI. Kemp and *A.P. Lille* for the Commissioner.

BEAUMONT, C.J.—Application No. 1074 of 1935 is an application to the Court asking us to direct the Commissioner of Income-tax, Bombay, to state a case raising a point of law under S. 66 (3), of the Income Tax Act. The point involved is a very short one. The assessee in partnership with his cousin carries on the business of money-lending, and until the accounting period, which is Samvat year 1988, ending in November 1932, the assessee's firm adopted what is known as the mercantile basis of accounting, that is to say, they showed the income accruing in

any year as being the income on which assessment was to be based, and not the income received during that year. Shortly before the accounting period in question the assessee and his cousin quarrelled. Litigation is going on for the partition of their estate and business, and the debtors of the firm refuse to pay interest, because they do not know which of the partners will ultimately be entitled to it. Consequently the actual amount received for interest is very much less than the amount shown in the books as accrued interest, and that being so, the assessee desires to change his method of accounting from the mercantile method to the cash method. The learned Commissioner has refused to accept that. I desire to say that I am not altogether in agreement with the reasoning on which the learned Income tax Commissioner bases his order. Section 13 of the Act provides that income, profits and gains shall be computed in accordance with the method of accounting regularly employed by the assessee. The Commissioner says that the regular method is the mercantile method, and he must adopt that. That may be so, but, at the same time, it seems to me impossible to contend that an assessee is never at libery to alter the regular method which he has once employed. What he must alter however is his regular method, that is to say, he must abandon what, up to that time, has been his regular method, and start a new regular method and not merely a new method for a casual period.

It seems to me plain that there must be a power to change, because supposing that an assessee were to keep his accounts on the mercantile basis down to the year 1930, and then for five years he were to keep his accounts on the cash basis, it could hardly be suggested that at the end of the five years his regular method of accounting was still the mercantile method. But if a change has been made, it must have been made at some definite moment of time. The learned Commissioner is however entitled to require proper evidence that the regular method of accounting has been changed. If the Commissioner is satisfied that at a particular moment the assessee has changed his regular method of accounting, he is not likely to be satisfied in the following year or a few years later, that the regular method has been changed again back to the old method. The assessee is not entitled to change his method of accounting from year to year as suits him

best; the reference in Section 13 to the regular method of keeping accounts precludes any practice of that sort. But although I think that the reasoning of the learned Commissioner is in some respects wrong, because he certainly seems to suggest that a method once regularly adopted can never be changed, I think the question of law which the assessee desires us to direct the Commissioner to raise does not really arise.

The question suggested is whether on a true construction of Section 13 of the Income tax Act, the Income tax Officer was wrong in law in not accepting the method of accounting employed by the assessee since Samvat year 1988. Now that question really involves an actual question of fact, and a hypothetical question of law. First of all, has the regular method of accounting been changed? That is a pure question of fact, and the only point of law would be a hypothetical one, namely, if the regular method has been changed, is the Commissioner bound to adopt that change? I do not suppose the learned Commissioner would dispute that he is bound to recognise a changed method, and the only real question is whether he ought, or ought not, to have been satisfied that the method has been changed, which, as I say, is a pure question of fact on which it is not open to us to differ from the learned Commissioner. In my view, therefore, there is no point of law which arises on the assessment which we can direct the learned Commissioner to raise. The application, therefore, must be rejected. With regard to Application No. 1075 of 1935, it is an application by the assessee in respect of the next following year. The same considerations apply, except that obviously it is rather easier to prove for the subsequent year that the regular method has been changed than it was for the earlier year, but no more law arises in the second application than the first. Therefore both applications must be rejected with costs on the original side scale to be taxed by the Taxing Master.

RANGANEKAR, J.—I agree but as the question of construction of Sec. 13 has been raised in the course of the discussion, I should like to state shortly my view of the section. The section says that income, profits and gains shall be computed for the purposes of Secs. 10, 11 and 12 in accordance with the method of accounting regularly employed by the assessee. It follows from that section that when an assessee says that the method which he has followed

has been regularly employed by him, the question whether that is so or not is entirely for the Income tax authorities, any opinion expressed by them would amount to nothing more than a finding of fact and would not entitle the assessee to come to this Court. But I do not agree with the Commissioner that it is not open to a person to change a method which he has regularly employed for some years at any period in any particular year. There is nothing in the section or the Act to prevent an assessee from changing his method. He has of course to satisfy the Income tax authorities that he is doing so in good faith, and if the revenue is not likely to be defrauded, I think the Income tax Officer will accept the new method, and if he refuses, his discretion can be questioned on an appeal to the superior officers.

Application rejected.

[IN THE SIND JUDICIAL COMMISSIONER'S COURT.]

JAMSHED SOHRAB KATRAK

v.

SECRETARY OF STATE FOR INDIA.

RUPCHAND BILARAM, A. J. C.

July 3, 1936.

FIRM—MINOR PARTNER—RIGHT TO CLAIM REFUND OF TAX UNDER SEC. 48 (2)—LAW BEFORE AMENDMENT ACT OF 1933—INDIAN INCOME TAX ACT (XI OF 1922), SEC. 48 (2).

Under the Indian Income Tax Act (XI of 1922) before Section 48 of the said Act was amended by Act XVIII of 1933, a minor who owned a share in a partnership which had been registered as a firm was not entitled to claim a refund on the ground that the rate of income tax applicable to his total income of the previous year was less than the rate at which income tax had been levied on the profits of the firm of that year. This omission has been set right by Act XVIII of 1933.

A minor cannot be 'a member of a firm', though he may be admitted to the benefits of a partnership.

Suits Nos. 49, 58, 114, 115, of 1934.

Suganlal Hassanand, for the plaintiffs.

Partabrai D. Panwani, for the Crown.

JUDGMENT.

The facts giving rise to these suits are not in dispute. It is common ground that on 14th May, 1931, the constitution of the assessee firm which carries on business in the name of Messrs. Katrak & Co., was changed and a partnership agreement was entered into on that date alloting equal shares to five persons, two of whom are minors. One of these minors is plaintiff in Suits Nos. 49 and 115 of 1934 and the other is plaintiff in Suits Nos. 58 and 114 of 1934. All of them are described in the deed as partners. An application was made to the Income Tax Officer, Karachi, to register the firm as now constituted under the provisions of Seclion 26-A of the Income Tax Act. The Income Tax Officer declined to register the firm on two grounds; first, that one of the alleged partners in the firm was a bogus partner, and secondly, the two others were minors and as such were in law not partners in the firm. He accordingly assessed the firm as an unregistered firm. On revision the Income Tax Commissioner passed the following order:—

"The income assessed is in order. The Income Tax Officer is directed to register the firm of Messrs. Katrak & Co., who should be assessed at the maximum rate on the total income."

The above order is dated 18th January, 1933. Accordingly it applied not only to the assessment leviable for the years 1931-32 but also for the years 1932-33. This order was duly given effect to and the assessment for both these years levied from the assessee firm at the maximum rate. All five persons mentioned in the partnership deed then applied under Section 48 (2) of the Act for refunds on their shares of profits in the assessee firm calculated at the difference between the maximum rate of income tax at which the firm was assessed and the rates at which their individual total incomes from all sources were chargeable. The Income Tax Officer rejected the application of the minor plaintiffs on the ground that under the law then in force no such refunds were permissible, and hence these suits. Now, it is well settled that although a minor may be admitted to the benefits of partnership in a firm, he is not in the eye of law a partner in that

firm. Section 48 (2) of the Income Tax Act has been amended by Act XVIII of 1933 and provides for a refund being allowed not only to a partner in a registered firm but also to a minor who has been admitted to the benefits of partnership in a firm, and the plaintiffs have, as a matter of fact, been allowed refunds during subsequent years. The dispute between the parties is confined to the years 1931-32 and 1932-33. Suits Nos. 49 and 58 relate to the year 1931-32 and the other two suits to the year 1932-33. Section 48 (2) as amended reads as follows :

"If a member of a registered firm (or any person who being a minor has been admitted to the benefits of partnership in such firm) satisfies the Income tax Officer or other authority appointed by the Governor-General in Council in this behalf that the rate of income tax applicable to his total income of the previous year was less than the rate at which income tax has been levied on the profits or gains of the firm of that year (or that his total income of the previous year was below the minimum chargeable with income tax) he shall be entitled to a refund on his share of those profits or gains calculated at the difference between those rates (or at the rate at which income tax has been levied, as the case may be)."

The portions in brackets referred to above were added by the amending Act. The short question which therefore arises is as to the true meaning of the expression "a member of a registered firm." It is contended on behalf of the plaintiff that this expression includes within its ambit, minors admitted to the benefits of partnership in a registered firm and that the amending Act conferred no new right upon minors, but by the introduction of adequate words expressed what was already implied and thereby set at rest the doubts which had been raised on that point in certain quarters. I am afraid there is no substance in this argument. Section 2, Clause (6 A) of the Income tax Act provides that in this Act the expression "Firm" shall have the same meaning as that given to it in the Contract Act, 1872. Section 239 of that Act defines "a firm" thus :

"Persons who have entered into partnership with one another are called a firm."

The chapter of the Contract Act, dealing with partnerships has been substituted by the Partnership Act, 1932.

Section 4 of that Act contains the following definition of a firm:

"Persons who have entered into a partnership with one another are called individually 'partners' and collectively 'a firm' and the name under which their business is carried on is called the "firm name."

So far as the point in issue in these suits is concerned there appears to be no difference between these two definitions, and whether the definition contained in Section 239 of the Contract Act or that contained in Section 4 of the Partnership Act applies, 'a member of a firm' means and can only mean a person who has entered into partnership with another person or persons. If a minor is incapable of entering into a partnership with another person or other persons he cannot be a member of a firm in which he is not a partner. That being so, there can be no question that under Section 48, Cl. (2), prior to its amendment by Act XVIII of 1933, a minor was not entitled to claim a refund. It is rather unfortunate that the legislature had made a serious omission in the old section in not providing for relief to minors who for the purpose of income tax stood on the same footing as adults, and who were admitted to the benefits of partnership in a firm although they did not thereby become partners in the eye of the law. This omission has now been set right by the amending Act. But I am afraid the duty of the Court is *jus dicere* and not *jus dare* and the Court must give effect to the law as it then stood. In the course of argument it was suggested that as the Income Tax Commissioner has ordered the firm to be registered under the Act he had impliedly admitted that all the persons described in the partnership agreement as partners were as a matter of fact partners in the firm, and that the Crown was therefore estopped from contending that the plaintiffs being minors were not as a matter of fact partners.

It was faintly suggested that had the firm as described in the deed not been registered as such, the adult partners would have claimed and obtained refunds on the footing that the share of each of them in the profits of the firm was 1/3rd and not 1/5th as had been claimed by them and allowed by the Income tax Officer in the present case. But there are several answers to that argument. In the first place the plea of estoppel has not been

raised in the pleadings and no application has been made for leave to amend the pleadings. In the next place, the order passed by the Income tax Commissioner on revision was perfectly correct. Three persons out of five were adults and they formed members of a firm. They were entitled to have their firm registered on the strength of the partnership agreement which operated as such so far as they were concerned, and there is nothing in the order of the Income tax Commissioner to suggest that he recognised the minor plaintiffs either as partners or as members of the registered firm. At first I was much impressed by the argument that it was inequitable that the Income tax Officer should have allowed refund to three partners on the footing of the shares of them being 1/5th and not 1/3rd notwithstanding the practice prevailing in the income tax offices prior to the amendment of the section which was to the contrary effect. But this argument was sufficiently met by the Crown by offering to adjust refunds on that basis, it being the case of the Crown that such an adjustment would not materially benefit the assessees. That offer was not accepted; and, therefore, apart from the question whether it was open to the plaintiffs to urge this argument on the pleadings, there is no scope even for the contention that the plaintiffs or as a matter of that the other persons mentioned in the deed as partners have been in any way prejudiced by the order of the Income tax Commissioner. As the plaintiffs have failed on this plea there is no occasion for me to consider the other defences raised on behalf of the Crown. All these suits fail and are dismissed with costs.

Suits dismissed.

[IN THE CALCUTTA HIGH COURT.]

NRISINGA CHANDRA NANDY, *In re.*

SIR HAROLD DERBYSHIRE, C.J., AND PANCKRIDGE, J.

July 29, 1936.

ALLOWANCES—BUSINESS EXPENDITURE—MANAGING AGENCY AGREEMENT—AGENT EMPOWERED TO CONDUCT BUSINESS, TO PAY CERTAIN SUMS TO PRINCIPAL AND TO RETAIN BALANCE AS REMUNERATION—LIABILITY OF PRINCIPAL TO PAY TAX ON ENTIRE PROFITS OF BUSINESS—SUMS RETAINED BY AGENTS—NOT ALLOWABLE DEDUCTION—INDIAN INCOME TAX ACT (XI OF 1922), Sec. 10 (2) (*viii-a*), (*ix*).

An agreement between the assessee of the one part and three persons of the other, provided that the assessee shall employ the latter as managers of a business owned by the assessee for a period of five years, that the managers shall carry on and conduct the business of the assessee and secure work for and on behalf of the assessee and that the managers shall pay to the assessee a certain percentage of the gross realisations and also a further sum of Rs. 1,000 per year and, after paying all the expenses of and incidental to the business, retain the balance to themselves as remuneration. In respect of the year of assessment the assessee received in accordance with the terms of this agreement Rs. 14,510, but income tax was levied on the assessee in respect of the whole of the profits of the business, namely, Rs. 45,082. The question being whether the assessee was liable to be taxed on Rs. 45,082 or only on Rs. 14,510:

Held, (*i*) *that the business in question was a business carried on by the assessee and not by the managers and the assessee was the person to be assessed in respect of the taxable profits of the business;*

(*ii*) *that the assessee was not entitled to deduct from the profits of the business, namely, Rs. 45,082, the sum retained by the managers, under Section 10 (2) (viii-a) of the Income Tax Act, inasmuch as, even assuming that such sum was bonus or commission, it was not "a sum which would not have been payable as profit or dividend if it had not been paid as bonus or commission" within the meaning of the said clause.*

(iii) that the sum retained by the managers under the agreement was not 'expenditure incurred solely for the purpose of earning profits or gains' within Sec. 10 (2) (ix) and was not allowable even under this clause; and income-tax was therefore rightly levied on the assessee on Rs. 45,082.

PANCKRIDGE, J.—Obiter : *It cannot be laid down that in no circumstances can persons be assessable in respect of profits of a business which is not a business owned by them. Chapter III of the Act is not controlled by Section 3.*

It cannot be said that a principal cannot properly be described as carrying on business through his agents merely because there is no provision in the agreement permitting the principal to interfere in the executive control of the business.

PONDICHERRY RAILWAY CO. *v.* COMMISSIONER OF INCOME TAX, MADRAS [58 I.A. 239; 54 Mad. 691] *applied.*

BEJOY SINGH DUDHURIA *v.* COMMISSIONER OF INCOME TAX, BENGAL (1933 I.T.R. 135; 60 I.A. 196; 60 C. 1029) *distinguished.*

The facts of the case are stated fully in the judgment.

S. N. Banerjee, K. Bose and *A. C. Sen* for the Assessee.

The Advocate-General (A. K. Roy), R. B. Pal and *R. C. Pal* for the Commissioner of Income Tax.

JUDGMENT.

DERBYSHIRE, C. J.—This is a Reference to this Court made by the Income Tax Officer, Burdwan-Birbhum, arising out of the assessment made in the year 1932-33 upon Nrisingha Chandra Nandy Chowdhury as an individual on income from money-lending business carried on by him at Baidyapur in the Burdwan District, a rice mill at Boinchee in the Hooghly District, a business in stevedoring and dubashing in Calcutta, money-lending business carried on by him at Deoghar in the Sonthal Parganahs and his income from other sources. It is the stevedoring and dubashing business in Calcutta which gives rise to the question which is asked by the Commissioner. This stevedoring and dubashing business was carried on under the name of Chatterji & Co., and the question asked of this court is—what is the income properly assessable to income-tax of the assessee in respect of the business of Chatterji & Co.?

The assessee for some years previous to 1931 was the proprietor of this stevedoring and dubashing business of Chatterji

and Co., and appears to have appointed Sarat Chandra Chatterji, Tulshi Charan Chatterji and Radha Charan Chatterji who are described as merchants and land-holders, as managers of this business and the Chatterjis appear to have acted as managers of that business under certain agreements made between them and the proprietor.

On the 16th of March, 1931, an agreement in writing was made between the assessee described as the proprietor of the business and the said three Chatterjis who were described as managers. In that agreement the previous agreements were referred to. Then the written agreement proceeds in its operative part—

"Now it is hereby Agreed and Declared as follows :—

"1. The proprietor shall employ the managers as managers of his said business for the said period of five years commencing from the said 1st day of Baisakh, 1338 B.S., and the said business shall continue to be carried on by the managers up to the end of the month of Chaitra 1337 B.S., by virtue of and under the said hereinbefore in part recited agreement dated the 13th day of April, 1930, and all the terms, conditions and stipulations therein contained including the clause about adjustment of accounts shall be deemed to apply thereto notwithstanding anything herein contained.

"2. The managers shall continue to carry on and conduct the business of the proprietor and secure all Stevedoring and Dubashing work for and on behalf of the proprietor in the name of his said firm of 'Chatterjee & Co.,' in respect of the following lines of Steamships and vessels;

(*i*) Ellerman Bucknall Steamship Co., Ltd.
(*ii*) Hansa Line.
(*iii*) Holland Britain Indian Line.
(*iv*) Norwegian Line.
(*v*) Swedish East Asiatic Company.
(*vi*) Roosevelt I. S. Company.
(*vii*) River Pilot Service.

"3. The managers shall be at liberty to secure at any time during the continuance of this agreement contracts for Stevedoring and Dubashing work in respect of any other line of steamships and vessels for and on behalf of the proprietor and in the name of his said firm of Chatterjee & Co.

"4. The managers shall after collecting all bills and outstandings of the said firm of Chatterjee & Co., in respect of Stevedoring works in ships and vessels (excepting Tally Clerks, salt and extra gangs and winchmen) pay to the proprietor 5 per cent. on the gross realizations and in respect of Dubashing works (with the exception of Captains and Gharry hire) 2½ per cent. on the gross realisations without any deduction or abatement, whatsoever. The managers shall also pay to the proprietor a further sum of Rs. 1,000 per year on or before the expiry of the last day of the month of Chaitra each and every Bengali year during the aforesaid period of five years the first of such annual payments to be made on or before the expiry of the last day of the month of Chaitra, 1338 B. S. The managers shall after paying all expenses of and incidental to the carrying on of the business of the said firm of Chatterjee & Co., including salaries of clerks assistants, supervisors and other employees, establishment, contingent and other extra expenses, if any and the payments to be made to the proprietor as hereinbefore provided retain the balance to themselves as and for their remuneration.

"5. The proprietor shall have the option to appoint an assistant to supervise and check the collection of all bills and outstandings of the said firm of Chatterjee & Co., and the managers shall pay to the proprietor the salary of such assistant at the rate of Rs. 50 per month over and in addition to the said yearly sum of Rs. 1,000 and 5 per cent. and 2½ per cent. hereinbefore mentioned.

"6. The assistant so to be appointed as aforesaid shall have free access at all times during office hours to all documents, papers, books of account, correspondence, vouchers, bills, etc., relating to the business of the said firm of Chatterjee & Co., and the managers shall forthwith give every facility in that behalf.

"7. If owing to any negligence or default on the part of the managers in carrying on the business of the said firm of Chatterjee & Co., there be any loss, the same shall be borne and paid by the managers and the proprietor shall not be liable to bear or pay the same or any part or portion thereof and the managers shall at all times indemnify and keep indemnified the proprietor against all such losses."

"8. During the continuance of this agreement the managers

shall have full power and authority to sign, endorse and negotiate all bills, cheques, etc., in the name of the said firm of Chatterjee & Co.

"9. During the continuance of this agreement the managers shall not directly or indirectly secure any business of Stevedoring or Dubashing with any new line of Steamship and vessels in their own name or in the benami of any person or persons for their benefit. Should the managers act in any way contrary to the provision hereinbefore contained, then and in such case, such business should belong to the proprietor and should be deemed to have been secured for his benefit and he shall be at liberty to forthwith determine this agreement without any notice and also to recover from the managers the sum of Rs. 20,000 as and by way of liquidated damages besides forfeiting the security deposit hereinafter mentioned."

"10. The sum of Rs. 6,000 deposited by the managers with the proprietor as and by way of security in pursuance of clause 9 of the said hereinbefore in part recited agreement dated the 13th April 1930, shall continue to remain in deposit with the proprietor as and by way security for the due performance and observance of the covenants and conditions hereinbefore contained and on the part of the managers to be performed and observed and they shall not be entitled to claim refund of the said deposit or any part or portion thereof so long as any claim of the proprietor under and by virtue of this agreement shall remain outstanding and unsatisfied with liberty to the proprietor to appropriate the same or any part or portion thereof in satisfaction of such claim if the same be not paid on demand. The proprietor shall also be at liberty to recover from the managers the balance, if any, of such claim by suit or otherwise."

"11. On the expiry of the month of Chaitra each and every year, the accounts of the business of the said firm of Chatterjee & Co., on the basis of the hereinbefore in part recited agreement of the 29th day of September, 1924, shall be adjusted and upon such adjustment, the managers shall be at liberty to withdraw their respective shares in the profits in terms of the said agreement and the proprietor shall likewise be at liberty to withdraw his capital and other moneys from the said business."

"12. On the expriy of the agreement either by effluxion of

time or by sooner determination thereof as hereinbefore provided, the manager shall be at liberty to retain any capital or other moneys that they might have brought into the said business after having paid the proprietor, any money or moneys for the time being due to him by the managers under and by virtue of this agreement provided always and it is hereby expressly agreed and declared that nothing herein or in the said agreement, dated the 29th day of September, 1924, contained shall be deemed to constitute a partnership between the proprietor and the managers and the terms, conditions and stipulations contained in the said agreement, dated the 29th day of September, 1924, shall be deemed to be in full force and binding on the parties so far as they are not inconsistent with or repugnant to or expressly superseded by the terms, conditions and stipulations herein contained."

Pursuant to that agreement the business of Chatterjee & Co., was worked. In respect of the year of assessment the assessee received in accordance with the terms of the agreement Rs. 14,510. In respect of the same year the full profit of the business was computed by the Income-tax Officer to be Rs. 45,082. The question is whether the assessee is to be assessed upon the profits of the business, namely, Rs. 45,082 or upon Rs. 14,510 which he actually received. The assessee contends that he is to be assessed upon Rs. 14,510 whereas the Income tax Officer contends that the assessee is to be assessed upon Rs. 49,082 which was the full profit of the business.

Section 3 of the Income Tax Act enacts:—

"Where any Act of the Indian Legislature enacts that income tax shall be charged for any year at any rate or rates applicable to the total income of an assessee, tax at that rate or those rates shall be charged for that year in accordance with, and subject to the provisions of this Act in respect of all income, profits and gains of the previous year of every individual, Hindu undivided family, company, firm and other association of individuals."

Section 6 of the Income Tax Act provides:—

" Save as otherwise provided by this Act, the following heads of income, profits and gains, shall be chargeable to income-tax in the manner hereinafter appearing, namely:—

(*i*) Salaries.
(*ii*) Interest on securities.
(*iii*) Property.
(*iv*) Business.
(*v*) Professional earnings.
(*vi*) Other sources."

The assessment here purports to have been made under the fourth heading " Business."

Sec. 10 (*1*) provides :—

" The tax shall be payable by an assessee under the head ' Business ' in respect of the profits or gains of any business carried on by him."

Section 10 (*2*) provides that such profits or gains shall be computed after making full allowance for

(*viii-a*) " any sum paid to an employee as bonus or commission for services rendered, when such sum would not have been payable to him as profits or dividend if it had not been paid as bonus or commission : "

" Provided that the amount of the bonus or commission is of a reasonable amount with reference to :—

(*a*) the pay of the employee and the conditions of his service;

(*b*) the profits of the business for the year in question ; and

(*c*) the general practice in similar businesses."

(*ix*) " any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits or gains :

Provided that nothing in clause (*viii*) or clause (*ix*) shall be deemed to authorise the allowance of any sum paid on account of any cess, rate or tax levied on the profits or gains of any business or assessed at a proportion of or otherwise on the basis of any such profits or gains."

The question here is whether the business of Chatterjee & Co. was carried on by the assessee ? The income-tax authorities say it was—that it was carried on by the assessee through the three Chatterjees who were his managers for the purpose of carrying on the business. The assessee contends that by the agreement of March 16th, 1931, he (the assessee) had handed over the business for the period under the agreement to the three

Chatterjis and that they were carrying on the business. To determine which of these two views is correct we must have regard to terms of the agreement of March 16th, 1931.

Cl. (1) provides that the proprietor shall employ the managers as *managers* of his said business for the said period of five years.

Cl. (2) provides that the managers shall continue to *carry on and conduct the business of the proprietor*, and secure all stevedoring and dubashing work *for and on behalf of the proprietor* in the name of his said firm of "Chatterjee & Co." in respect of certain lines of steamships and vessels.

Cl. (3) of the agreement provides that the managers shall be at liberty to secure at any time during the continuance of this agreement contracts for stevedoring and dubashing work in respect of any other line of steamships and vessels *for and on behalf of* the proprietor and in the name of his said firm of Chatterjee & Co.

Cl. (4) provides that the managers shall pay to the proprietor five per cent. on the gross realizations in respect of dubashing works and two and half per cent. on the gross realizations in respect of stevedoring works and also a further sum of Rs. 1,000 and that after paying all expenses of and incidental to the carrying on of the business of Chatterjee & Co., they shall retain the balance to themselves as and for their *remuneration.*

Cls. (5) and (6) give the right to the proprietor to supervise and check the collection of all bills and outstandings of the firm of Chatterjee & Co.

Cl. (7) provides for the managers indemnifying the proprietor if owing to any negligence or default on the part of the managers in carrying on the business of Chatterjee & Co., there be any loss.

Cl. (8) provides that the managers shall have full power and authority to sign, endorse and negotiate all bills and cheques in the name of the said firm of Chatterjee & Co.

Cl. (11) provides for an accounting for what is due to the proprietor and what is due to the managers each year.

Cl. (12) provides that the managers shall be at liberty to retain any capital or other moneys that they might have brought into the concern and also that nothing in the agree-

ment shall constitute a partnership between the parties to the agreement.

This agreement, in my view, looking at it as a whole, is simply an agreement between the proprietor—the assessee—and the managers—the three Chatterjis—whereby the proprietor appointed the three Chatterjis as managers of the business for five years, the business at all times remaining as that of the proprietor, the proprietor taking out of the business, as stated, each year a sum of Rs. 1,000 fixed, five per cent. of the gross realisations in respect of the stevedoring work and two and half per cent. in respect of the dubashing work with a provision that the balance after paying all expenses should be the remuneration of the managers. It was in my view an agreement whereby the managers should on those terms carry on the business on behalf of the proprietor. The business at the beginning was that of the proprietor; during the continuance of the agreement it should be that of the proprietor and at the end it should be that of the proprietor. The Chatterjis were simply the managers managing the business for and on behalf of the proprietor. That being so, it seems to me that the proprietor—the assessee—was through his managers—the three Chatterjis—carrying on the business and that consequently he falls to be assessed under sec. 10 (1) of the Indian Income Tax Act.

What is the sum in respect of which he is to be assessed? It is the profits or gains of that business subject to those profits or gains being computed after making the allowance set out in sec. 10 (*2*) (*viii-a*) or (*ix*). The whole profits in this case are Rs. 45,082. It is contended on behalf of the assessee that under sec. 10 (*2*) (*viii-a*) or 10 (*2*) (*ix*) a deduction or allowance should be made from that sum in respect of the Chatterjis for the services they have rendered. It is suggested that this sum should be evaluated at the difference between Rs. 45,082 and Rs. 14,510. It is contended that that difference represents bonus or commission for the services Messrs. Chatterjis have rendered; in other words that the proprietor would have had to pay that sum to any manager for the purposes of running the business so as to earn the profit of Rs. 45,082. It is doubtful whether this sum, which in the agreement is called remuneration, is either bonus or commission for services. If it is not bonus or commission it

is not deductible. If it is bonus or commission, Sec. 10 (*2*) (*viii-a*) provides that any sum so allowed is only to be allowed when such sum would not have been payable to the employee as profits on dividend as it had not been paid as bonus or commission. In this case the sum in question has been allowed under the agreement so that it is not permissible to allow the deduction in question under Sec. 10 (*2*)(*viii-a*).

It is next contended that a similar sum should be allowed under Sec. 10 (*2*) (*ix*). It must be remembered that this sum is a share of the profit and if allowed would be deemed to be a payment out of the profits. That position was considered by the Privy Council in the case of the *Pondicherry Railway Co., Ltd.* v. *The Commissioner of Income Tax, Madras,* and in the judgment which was delivered by Lord Macmillan it was said:

"A payment out of profits and conditional on profits being earned cannot accurately be described as a payment made to earn profits. It assumes that profits have first come into existence. But profits on their coming into existence attract tax at that point and the revenue is not concerned with the subsequent application of the profits."

Later in the same judgment his Lordship cited the words of Lord Halsbury in *Gresham Life Assurance Society* v. *Styles* where Lord Halsbury said:

"The thing to be taxed is the amount of profits or gains. The word 'profits' I think is to be understood in its natural and proper sense which no commercial man would misunderstand. But when once an individual or a company has in that proper sense ascertained what are the profits of his business or his trade, the destination of those profits or the charge which has been made on those profits by previous agreement or otherwise is perfectly immaterial. The tax is payable upon the profits realized and the meaning to my mind is rendered plain by the words 'payable out of profits.'"

Having regard to those words, it seems to me impossible to say that the allowance claimed can be made under Sec. 10 (*2*) (*ix*). Therefore the answer to the question put by the Commissioner to the Court is that the income properly assessable to income tax of the assessee in respect of the business of Chatterji & Co.,

is the sum of Rs. 45,082 which was computed by the Income tax Officer to be the full profits of the business.

I must say that I have come to this conclusion with considerable reluctance, because it appears to me that the assessee is being assessed to tax upon a sum of money which he never received in full and which he was not entitled to receive in full. But such is the operation, in my view, of the income tax law in this particular case. The assessee has unfortunately made an agreement for the division of the trading surplus of his concern as between himself and his managers without having regard to the incidence of income tax as laid down by the law.

The Income tax Commissioner is entitled to his costs—seven gold mohurs to Mr. Pal instructing the Advocates in this case. The fees for the Advocates appearing will be taxed in the same manner as of hearing of an appeal from a decree on the Original Side.

PANCKRIDGE, J.—I am of the same opinion.

At first it appeared to me that some difficulty might be caused by the fact that no part of the profits as such was received by the assessee. Under Sec. 3 of the Indian Income Tax Act a tax at the appropriate rate is charged subject to the provisions of the Act in respect of all income, profits, and gains of the preceding year of every individual, Hindu undivided family, company, firm and other association of individuals.

In *Raja Bejoy Singh Dudhuria v. Commissioner of Income-Tax, Bengal,* Lord Macmillan in delivering the judgment of the Judicial Committee observed at page 200 (of 60 I. A.):

"When the Act by Sec. 3 subjects to charge 'all income' of an individual, it is what reaches the individual as income which it is intended to charge."

Having regard to those observations and the words of Sec. 3, I was disposed to think that it was possible that the provisions of Chapter III of the Act were to some extent limited by Sec. 3. If that were so, it is possible that the profits or gains of any business carried on by an assessee would not be taxable unless they were his profits or gains within the meaning of Sec. 3. I have come to the conclusion, however, that no such difficulty arises and that the provisions of Chapter III must be construed as they stand.

For example, it is clear that under Sec. 9 an assessee is liable in respect of the annual value of property of which he is the owner although in the year in question he has, in fact, derived no income or other profit or advantage from his ownership. There is accordingly no difficulty in arriving at the conclusion that the assessee in this case is liable to be taxed on the profits or gains of the business of Chatterjee & Co., if that business can properly be said to be carried on by him within the meaning of Sec. 10 (1). The section does not require that the business should be carried on by the assessee personally. Indeed, in modern commercial conditions businesses are often carrid on by agents entrusted with wide powers by their principals, with whom regular communication is not practicable. To arrive at the conclusion whether or not the business in this case was carried on by the assessee, it is necessary to examine the agreement of the 16th of March, 1931. I have no doubt that in Sec. 10 (1) the Legislature contemplated that the business carried on by the assessee was the assessee's business. At the same time I do not wish it to be thought that I express the opinion that in no circumstances can persons be assessable in respect of profits of a business which is not a business owned by them.

When I turn to the agreement, I find that the first clause in it is that the proprietor shall employ the managers as managers of his business for a period of five years. To my mind those words are apt to express an agreement by one party to employ another as agent to carry on the business belonging to the first party. If that is the legal position established by this agreement then, in my opinion, the assessee can rightly be described as carrying on the business, although he carried it on, not personally but through his agents.

The second clause appears to me to emphasize this aspect of the relationship, for that clause provides that the managers shall continue to carry on and conduct the business of the proprietor and secure all stevedoring and dubashing work for and on behalf of the proprietor in the name of his firm "Chatterjee & Co." in respect of the specified lines of steamships.

The third clause gives the managers liberty to secure contracts with other lines of steamships for and on behalf of the proprietor and in the name of the firm of Chatterjee & Co.

The assessee attaches considerable importance to the fact that under the agreement he has no control of the conduct of the business. I will assume that this is so, although I may observe that there is no covenant on his part to abstain from interfering with the business and, as has been pointed out, he could at any time revoke the authority of the managers, although if he did so without justification he would be liable to make compensation by reason of the provisions of Sec. 205 of the Indian Contract Act. Moreover, in the case of a breach of one of the covenants entered into by the managers, the proprietor has the right to determine the agreement and to recover a sum of money by way of liquidated damages. In any event, however, I do not think that it can be said that the principal cannot properly be described as carrying on business through his agents merely because there is no provision in the agreement permitting the principal to interfere in the executive control of the business. I accordingly agree with my Lord the Chief Justice that this is a "business carried on by the assessee" and that tax is payable by him in respect of the profits and gains of the business.

With regard to the claim of the assessee, on the assumption that he is liable to be assessed, to deduct the difference between the sum payable to him under the agreement and the net trading profits of the business under Sec. 10 (*2*) (*viii-a*) or, alternatively, under Sec. 10 (*2*) (*ix*), I am of opinion that the contention cannot prevail. It is not argued that payment of the balance of the profits under cl. (4) of the agreement is a "bonus" within the meaning of sub-cl. *(viii-a)*. I should find some difficulty in holding that they were commission, for the question naturally arises—commission upon what? Personally I should find great difficulty in holding that the balance of the profits could be properly described as commission upon the profits. Apart from that I agree with my Lord that the sub-clause cannot apply because the net profits after payment of the expenses and the sums due to the proprietor under the agreement are payable under cl. (4) to the managers. In these circumstances, in my opinion, the condition that the commission must not be payable to the employee as profit or dividend if it has not been paid as commission is not fulfilled.

With regard to sub-cl. (*ix*), after the observations of the Judicial Committee in the case of *Pondicherry Ry. Co.* v. *Commissioner of Income-tax, Madras*, it is quite impossible to hold that the remuneration of the managers can be described as "expenditure incurred solely for the purpose of earning profits or gains." To my mind it is absurd to say that the whole or any part of the profits can be expenditure for the purpose of earning profits.

In these circumstances, I agree that the question propounded by the Commissioner of Income Tax, Bengal, should be answered in the manner formulated by my Lord.

Reference answered accordingly.

THE

INCOME TAX REPORTS

VOL. IV

1936

ENGLISH CASES

[IN THE HOUSE OF LORDS].

WILLIAMSON *v.* OUGH (INSPECTOR OF TAXES).

THE LORD CHANCELLOR (VISCOUNT HAILSHAM), LORD BLANESBURGH, LORD RUSSELL OF KILLOWEN, LORD MACMILLAN, LORD ROCHE.

March 2, 1936

INCOME TAX—WILL—POWER TO ADVANCE SUMS OUT OF CAPITAL OF TRUST FUND ON ACCOUNT OF INCOME—TO BE CHARGED AGAINST INCOME—ANY PAYMENT OUT OF CAPITAL TO BE RECOUPED —ENGLISH INCOME TAX ACT, 1918 (8 & 9 GEO. 5. c. 40), CASE III, SCHED. D.

A testator by clause 16 of his will declared that the trustees of his will might make payment on account of income to beneficiaries under the trust fund notwithstanding that the trustees might have no, or not sufficient, income in their hands and that such payments might be made out of any money for the time being in the hands of the trustees, whether representing capital or income of the trust fund, but so that the same should be duly charged against income and any payment made out of capital should, so far as practicable, and as and when his trustees should think proper, be duly recouped. The trustees, with the authority of an order of the Court, exercised their powers under clause 16 by raising a sum of £10,000 from their bank, on the security of 78,912 £1 ordinary shares in a colliery company which formed

part of the capital of the estate, and paid to the appellant in the tax year ending April 5, 1928, £2,000 in several instalments, and £500 in the year 1928-1929. Income tax was not deducted in making these payments and no recoupment had been made. The commissioners of income tax, and the special commissioners, held that under the terms of the will the appellant was only entitled to receive income, and the payments so made to her out of the capital of the estate were income in her hands and liable to taxation. Finlay, J., reversing those decisions, held that the payments were loans to her, repayable by her. The Court of Appeal (Romer, L.J., dissenting), allowed an appeal, on the ground that the money so paid did not constitute a loan, or give rise to a debt from the appellant to the trustees, but was income in her hands :— Held, *that clause 16 meant that sums could be paid out of capital to life tenants, and that the only recoupment was to be made out of future income, in the discretion of the trustees. Therefore there was no basis on which to establish personal liability, either expressly under the clause or by implication under the general law. A payment out of corpus might properly be assessable income in the hands of the recipient.*

Decision of the COURT OF APPEAL (151 L. T. 450) *affirmed.*

Appeal from the judgment of a majority of the Court of Appeal (Lord Hanworth, M.R., and Slesser, L.J.); Romer, L.J., dissenting.

The material facts are set out above in the headnote and are more fully stated in the judgment of Lord Russell of Killowen, with which the other noble and learned Lords concurred.

Radcliffe, K.C., and *John Sparrow*, for the appellant.

The Attorney-General (*Sir Thomas Inskip K.C.*), *J.H. Stamp* and *Reginald P. Hills*, for the respondent.

The arguments sufficiently appear from the judgment.

The House took time for consideration.

March 2.—LORD RUSSELL OF KILLOWEN.—I am authorised to say that my noble and learned friends, the Lord Chancellor, Lord Blanesburgh and Lord Roche, concur in the opinion which I am about to deliver.

The question here in dispute is whether the appellant is liable to be assessed to income tax in respect of two sums of £2,000 and £500, the assessments being made upon her under Schedule

D of the Income Tax Act, 1918, for the years ending April 5, 1928, and April 5, 1929, respectively.

The appellant's father Charles Edward Hunter, died on May 16, 1917. By his will he appointed his wife, Mary Emma Hunter, and two other persons his executors and trustees, and by the joint operation of clauses 8 and 9 thereof bequeathed free of duty to his wife an annuity of £ 6,000 for her life, payable quarterly, to be a charge on the residue of his estate, unless and until an annuity fund to provide for it was constituted by the trustees of the will. By clause 11 the testator devised and bequeathed to his trustees all the residue of his real and personal estate not otherwise specifically disposed of by his will upon the usual trusts for sale and conversion; and after usual directions for payment of funeral and testamentary expenses and debts and pecuniary legacies, he—by clause 13—directed his trustees to stand possessed of his residuary trust fund and the annual income thereof (*a*) upon certain trust for accumulation of surplus annual income exceeding £20,000 during the first fourteen years after his death, which are not material hereto, and subject thereto (*b*) during the lifetime of his wife upon trust to divide and pay the income of the trust fund equally between his wife and such of his three daughters, the appellant, Mrs. Kathleen Carp Elwes and Lady Sylvia Grant-Lawson, as for the time being should be living issue, as therein directed, and (*c*) after the death of his wife upon trust as to both capital and income for the testator's three daughters in equal shares, the share of each daughter being settled upon trusts for her and her issue.

By clause 16 the testator conferred the following power on his trustees; "During the lifetime of my wife my trustees may at their discretion make payment on account of income to the persons for the time being entitled to the income of the trust fund notwithstanding that my trustees may have no available income in their hands or not sufficient for the purpose, but such payments in advance of income received shall not exceed £500 for each quarter of a year in respect of each share of income, and such payments may be made out of any money for the time being in the hands of my trustees, whether representing capital or income of the trust fund, but so that the same shall be duly

charged against income and any payment made out of capital shall so far as practicable and as and when my trustees shall think proper be duly recouped."

By clause 20 the testator declared that notwithstanding the trust for sale and conversion of his residuary estate contained in his will his trustees might if they thought proper raise any sum or sums for any purpose of or under his will, "including the payment under clause 16 hereof of any sums in advance of income" by mortgage or charge of any part or parts of his estate.

The testator was survived by his wife and his three daughters. By the year 1927 the income of the residuary trust fund—which consisted in large part of colliery shares—had become so reduced that the beneficiaries were left practically without income therefrom. In those circumstances the trustees—with the authority of an order of Court—exercised their powers under clause 16 of the will. They raised a sum of £10,000 from their bank on the security of certain colliery shares which formed part of the capital of the estate. Out of the moneys so raised they paid to the appellant £2,000 during the financial year ending April 5, 1928, and £500 during the next financial year. These are the payments which are the occasion of the present dispute. Similar payments were made to the widow and the other two daughters.

The appellant, having been assessed to income tax in respect of these two sums, appealed; but the special commissioners confirmed the assessments, and on the requirement of the appellant stated and signed a Case—dated November 1, 1933—for the opinion of the High Court.

Before the Case came before the High Court for hearing, the testator's widow died and the annuity of £6,000 per annum payable to her under his will thereupon ceased. At the date of her death there were unpaid arrears of her annuity amounting to £2.800 1s. 4d., but, on the other hand, no recoupment had taken place in respect of the £2,500 paid to her under clause 16 of the will. The trustees of the testator's will accordingly took out an originating summons in the Chancery Division raising the question whether the unpaid arrears of annuity in their hands were applicable by them (*inter alia*) in discharging one-

fourth of the debt of £10,000 and the unpaid interest and bank charges thereon. By his order made on the hearing of that summons dated November 30, 1933, Bennett, J., declared that the unpaid arrears of the annuity were so applicable. The Stated Case was heard by Finlay, J., who by his order dated March 28, 1934, reversed the determination of the commissioners. The present respondent then appealed to the Court of Appeal, and by an order of that Court—dated June 28, 1934—the appeal was allowed and the determination of the special commissioners was restored. Romer, L. J., however, delivered a dissenting judgment.

The Master of the Rolls and Slesser, L.J., both were of opinion that under clause 16 of the will the trustees were empowered to make payments to the beneficiaries so as to secure them an income in any event, that the payments did not create any debt from them, and that the provision for recoupment merely enabled the trustees, if they thoughtfit, to replace out of future income capital which had been used in making payments under the clause. The payments were accordingly income in the hands of the present appellant. I agree with this construction of the clause.

The judgments both of Finlay, J., and Romer, L.J., are based upon the view that there was a personal liability upon the appellant to repay the moneys paid to her by the trustees in exercise of the powers conferred by clause 16. Finlay, J., puts it thus: "I have come to the conclusion, and in so deciding I think that I am deciding in accord with the view expressed by my brother Bennett that this money was money which the trustees were entitled to reclaim. . . . The lady was entitled to . . . income. The source temporarily dried up. Therefore in order to tide her . . . over what was obviously an embarrassing position, it was arranged that she should be given not income but a loan to be repaid if circumstances arose which made it possible that it should be repaid." Though Finlay, J., leaves it uncertain when repayment could be exacted, the relation of debtor and creditor is made clear.

Romer, L.J., arrives at the conclusion that any beneficiary, who has received payments from the trustees in the exercise of the powers conferred by clause 16, is personally liable to repay

to the trust estate the amount by which on her death it is ascertained that the payments which she has received from the income of residue and the receipts under clause 16 exceed her share of the income actually earned by residue during her life. This liability arises, according to him, not under the words of the clause, but by general law the operation of which was not excluded by the clause. "I see nothing in those words", he says in reference to the recoupment provision, "to exclude the case from the ordinnary operation of law, which would create an obligation to repay a sum paid in advance of income when it appears in the end that the sum so advanced exceeds the income to which the person who obtains the advance was entitled." This view of the Lord Justice that an obligation to repay arose from operation of law, is founded upon the construction which he placed upon clause 16, and can, I think, only be supported if that construction is right. It is the keystone of the judgment.

The construction which he placed upon the clause can best be stated in his own words: "The clause", he says, "does not in my opinion enable those beneficiaries to receive one penny more of income from the estate than they would in its absence; that is to say, it does not entitle them in the end to receive one penny more in respect of income from the testator's estate than they would in the absence of the clause." If this be the true view, it may be—I say no more than that—that the law would imply a personal liability to repay. But if the clause on its true construction means that sums can be paid under it out of capital to life tenants, and that the only recoupment to capital is to be made out of future income in the discretion of the trustees, there is no basis on which to establish personal liability, either expressly under the clause or by implication under the general law.

In my opinion that is the true construction of clause 16. It empowers the trustees when income is not available to provide out of capital payments to a limited amount to supply the place of the absent income. The payments, however, are to be "duly charged against income", that is to say, each life tenant is to be debited in her income account with the moneys which she receives under the clause; and in addition there is the provision as to recoupment which only requires recoupment "so far as practicable", and further only "as and when my trustees shall think

proper ". These words appear to me to exclude all idea of a personal liability to repay attaching to the recipient; they leave the corpus of the share to bear the burden, unless future income becomes available and the trustees deem it proper to recoup corpus thereout.

I think it true to say that the existence of this personal liability was not the principal argument of the appellant in your Lordships' House; but I have dealt with it first because, as I conceive, it was the foundation of the judgment in favour of the appellant. The main argument here was that if—without any personal liability—there existed a liability so to speak *in rem*, that is to say, that if the payments made under clause 16 were made upon the footing that the future income of the recipient under the trust might be taken to recoup capital, then the payments so made could not form income in the hands of the appellant assessable to income tax. No authority was cited in support of this contention; and I know of no legal principle to justify it. It is well settled that a payment out of corpus may properly be assessable income in the hands of the recipient. A familiar instance is the case of an annuity charged on the income and corpus of an invested fund; all moneys raised out of corpus to provide the amount of the annuity will be assessable income. The present case presents a close analogy; for clause 16 in effect if and when the trustees choose to exercise their powers thereunder, secures to the life tenants an income from residue by means of a charge on the corpus thereof.

In my opinion the appellant has been rightly assessed and this appeal should fail.

Lord Macmillan.—My Lords, I am in entire agreement both with the reasoning and with the conclusion of my noble and learned friend Lord Russell of Killowen.

Appeal dismissed.

Solicitors—Ellis, Peirs & Co., for appellant; Solicitor of Inland Revenue, for respondent.

[IN THE HOUSE OF LORDS].

JOHN EMERY & SONS *v.* LORD ADVOCATE.

LORD BLANESBURGH, LORD ATKIN, LORD THANKERTON, LORD MACMILLAN, LORD MAUGHAM.

May 26, 1936.

INCOME TAX—BUILDER—SALES IN CONSIDERATION OF GROUND ANNUALS—PROFITS ON PURCHASE AND RE-SALE OF BUILDING FEU—REALISABLE VALUE OF GROUND ANNUAL PART OF PROFITS AND GAINS IN COMPUTING TRADE PROFITS—ENGLISH INCOME TAX ACT, 1918 (8 & 9 GEO. 5. 40), SCHED. D.

The appellants, who carried on the business of builders and dealers in real estate, bought certain land, built houses upon it and disposed of their entire interest in the land for cash and for certain ground annuals. The land thereby became subject to what in England would be called a rent charge, and the ground annuals did not become a personal obligation of the purchasers, but an annual charge which could be realised out of the land, and the right of the appellants was a realisable right—a market security :—
Held, that the value of that marketable security must be brought into account for assessing the profits made in the particular year of trade for the purposes of income tax. The judgment in the First Division of the Court of Session expressed the opinion of the House.

Decision of the COURT OF SESSION, *sub nom.* EMERY *v* INLAND REVENUE COMMISSIONERS [1935] S. C. 802; [1935] Sc L. T. 501), *affirmed.*

Appeal from the judgment of the First Division of the Court of Session (Scotland).

The material facts are set out shortly in the headnote.

James Keith K.C. (*Dean of Faculty*) (of the Scottish Bar), *Needham, K.C., Scrimgeour* and *John Wheatley* (of the Scottish Bar), for the appellants.

The Attorney General (*Sir Donald Somervell, K.C.*), *the Lord Advocate* (*T. M. Cooper, K.C.*), *the Solicitor-General for Scotland* (*Albert Russell, K.C.*), *Reginald P. Hills* and *T. B. Simpson* (of the Scottish Bar) for the respondent.

At the conclusion of the arguments on behalf of the appellants, counsel for the respondent being present but not called on, their Lordships delivered judgment as follows:

Lord Blanesburgh—Notwithstanding the careful, full and able arguments which your Lordships have heard on behalf of the appellants, I believe you are all of opinion that the judgments in this case which were delivered in the First Division of the Court of Session stand undisturbed. They express my own view quite truly, and I do not feel that I could usefully add anything to them. This appeal must, I think, be dismissed, and I move your Lordships accordingly.

Lord Atkin.—I agree that this appeal should be dismissed, and for the reasons which have been given in the Court of Session.

Put quite simply, the position is that the appellants, who carried on the business of builders and dealing in real estate, entered into a transaction, or two transactions, by which they bought certain land, built houses upon it, and—without going into detail—disposed of their entire interest in the land for cash and for certain ground annuals. The position of the ground annuals seems to be this, that there was an obligation created in the several purchasers of the land by which the land became subject to what we in this country should call a rentcharge, which was not a personal obligation of the purchasers, but which was an annual charge which could be realised out of the land—a real burden upon the land. It is established that that obligation, or that right on the part of the appellants, was a realisable right, a market security in the sense of something which they could have realised at any moment by going into the market.

In those circumstances the case appears to me to be as plain as could be. It is a case where people have sold in the course of business part of their stock for money plus money's worth, namely, the equivalent of a marketable security. The position in respect of ground annuals appears to me to be precisely the same as though they had sold the land for money plus an annuity or plus a bond conditioned for the payment of these particular sums, or for debentures under which those sums were payable annually; it could be put in a great many different ways. However you put it, the result is not that they exchange part of their

stock for a different kind of stock, but that they dispose of the whole of their stock for money plus money's worth. In those circumstances it seems to me on the plainest principles that the value of that marketable security has to be brought into account for the purpose of assessing the profits which they made in the particular years of trade. Those appear to be the principles upon which the Court of Session proceeded. It appears to me that they are right, and I concur in the motion which has been proposed.

LORD THANKERTON.—I concur. The first important point to observe in this case, to my mind, is that the transactions in question were admittedly part of the ordinary trading of this particular company; and secondly, as the learned Dean of Faculty admitted, that the transactions between the appellants as sellers of the houses and land, and the buyers of the houses and land, were completed transactions of sale. Then it needs to be observed: What did the appellants get as the consideration for the sale? They got two things: they got sums of money, and they got the obligations—the real burdens—in the nature of ground annuals which had been constituted by them in the course of the transactions. I have difficulty in seeing, even on counsel for the appellants' argument, how in any real sense you can arrive at the cost of those ground annuals; and on the other hand, it is perfectly clear, and must have been familiar to these appellants as to anybody else in Scotland, that ground annuals such as these have a well-known market value, and that they are constantly traded in, and in that respect they seem at least as good money's worth as any ordinary security quoted on the stock exchange. It does seem to me that the proper view of that part of the transaction is that in effect the appellants agreed to leave part of the price as a real burden on the property to the extent of the well-known marketable value or thereabouts at the time. The main argument of the learned Dean of Faculty was that you could not bring this in until they realised it, as he admitted they could do, in the market. That in itself seems to me to amount at once to an admission that there was money's worth received at the time when the transaction of sale was completed, and if part of the price paid for the land and buildings consisted of money's worth, the

marketable value of which asset is immediately ascertainable, I fail to see why that should not be brought into computation in the ordinary accounts of the trader for the purpose of bringing out the results of his year's trading. Finally, I may say that I agree generally with the opinions of the Lord President in the Court below, and I concur in the motion which has been proposed.

LORD MACMILLAN.—Your Lordships who have preceded me have so clearly set out the reasons which satisfy me that the judgment below was right that I have nothing to add except to express my agreement.

LORD MAUGHAM.—I will add only a very few sentences to what has fallen from your Lordships, with which I entirely agree.

I think Lord Fleming was right when in his opinion he used these words: "The tax-payers' counsel in the course of his argument said, and I assume he was right in saying, that, if a house had not been sold, the tax-payers would not have been obliged to enter its value in their accounts as an item received by them." The emphasis there is, however, on the word "value". Lord Fleming did not, I think, mean that nothing ought to be entered in their accounts, and it would no doubt have been right in that case to enter the houses which were not sold at cost or market value, whichever was the lower. Then he goes on to say: "But the point of the case, to my thinking, is just that the houses were sold and that the taxpayers parted completely with the right of ownership in them." It is precisely for that reason that there is no ground for putting an artificial cost of production, so to speak, on the ground annuals which have been obtained as the result of the sale of this property, since the ground annuals have definite market value which can readily be ascertained. I agree with what has been said, that the right of ownership has, by the transaction in question, been converted into a different type of property, namely, ground annuals.

On those grounds I am satisfied that the opinions of the learned Judges of the Court of Session are perfectly correct.

Appeal dismissed.

[IN THE HOUSE OF LORDS.]

MONTAGUE BURTON, LTD. (*in liquidation*)
v.
INLAND REVENUE COMMISSIONERS.

THE LORD CHANCELLOR (VISCOUNT HAILSHAM),
LORD BLANESBURGH, LORD RUSSELL OF KILLOWEN,
LORD MACMILLAN, LORD ROCHE.

Feb. 6, 1936.

COMPANY—DISTRIBUTION OF REASONABLE PART OF INCOME—POWER OF SPECIAL COMMISSIONERS TO DIRECT INCOME TO BE DEEMED INCOME OF MEMBERS FOR PURPOSES OF SUPER-TAX—COMMISSIONERS TO HAVE REGARD TO CURRENT REQUIREMENTS AND MAINTENANCE AND DEVELOPMENT OF BUSINESS—MORE THAN PROFITS OF YEAR USED IN BUSINESS—FINANCE ACT, 1922 (12 & 13 GEO. 5. C. 17), s. 21.

The income tax commissioners found that the appellant company had for the income tax year in question expended on the current requirements of its business, and other requirements advisable for the maintenance and development of that business, amounts far in excess of the profits of the year, and that the company's business had been so carried on as to bring it within the purview of Section 21 of the Finance Act, 1922, so that for purposes of super-tax of the members of the company the income of the company for the year in question must be deemed to be the income of the members. The special commissioners, the Board of Referees and Finlay, J., and the Court of Appeal confirmed their decision :—Held, *that there was evidence upon which the commissioners could find that the company had not distributed a reasonable part of its income, and that therefore it came within the purview of Section 21. The direction in the proviso to Section 21 was that one of the relevant factors to which attention must be paid by the commissioners and by the Board of Referees was the fact that the income, or sums equivalent to the income, had been spent on requirements necessary or advisible for the maintenance and development of the business; but the proviso did not mean that wherever that happened, then, whatever the facts were,*

the commissioners were bound to hold that the requirements of Section 21 had not been complied with.

Decision of the COURT OF APPEAL (152 L.T. 8), *affirmed.*

Appeal from a judgment of the Court of Appeal on July 4, 1934 (Lord Hanworth, M.R., Slesser, L.J., and Romer, L.J.).

The facts are set out in the judgment of the Lord Chancellor.

The arguments, which appear from the judgment of the Lord Chancellor, were heard on February 4 and 6.

Sir William Jowitt, K. C., Radcliffe, K.C., and *Frederick Grant*, for the appellants.

The Attorney-General (*Sir Thomas Inskip, K.C.*), *the Solicitor-General* (*Sir Donald Somervell, K.C.*), and *R.P. Hills*, for the respondents.

The House took time for consideration.

February 6.—THE LORD CHANCELLOR —This is an appeal from an order of the Court of Appeal affirming a decision of Finlay, J. Finlay J., had answered in the affirmative a question put to him by the Board of Referees, whether there was evidence upon which that Board could come to the determination which they actually reached confirming a direction of the special commissioners as to the proper method of dealing with the income of the appellant company under provisions of the Finance Act, 1922.

From the Case stated by the Board of Referees we find that the appellant company was formed in the year 1917 to take over a business of the manufacture of clothing and tailoring which was previously carried on by Sir Montague Burton, then Mr. Burton. At the time when the company was formed in 1917 the capital was £ 5,002, there were creditors to the amount of £ 13,510, there was an overdraft of about £ 9,500 and in that year there was a total profit of £ 2,025. During the next twelve years the company prospered exceedingly and continued to grow in a very remarkable manner. In the year 1929 we find that the capital had grown to £ 47,002, the creditors had increased to £ 633,436, there were £ 212,867 of bills payable, there was an overdraft of £ 1,342,595, and there was a balance standing at the credit of profit and loss account of £ 1,643,235.

It appears that the method adopted for financing the business

consisted partly of borrowing money from the bank and partly of lending money to Mr. Burton, who then bought long leasehold or freehold premises which were suitable for the shops which the company desired to acquire, and let the shops so acquired to the company. In the case of short leasehold only, the company, itself seems to have acquired the premises; in the other cases they lent money to Mr. Burton, Mr. Burton bought the premises and let them to the company, and the company then spent sums of money in equipping them for the purposes of its business.

In February, 1929, the directors of the appellant company determined to sell their business to a big public company. Accordingly agreements were entered into between the new company and the old company and between Mr. Burton and the new company whereby the shops of the old company were transferred to the new company; the old company was to be treated as having carried on business since April 1, 1928, for the benefit of the new company, and the old company retained as one of its assets the debt owing to it by Sir Montague Burton. That arrangement having been come to in February, 1929, the sales and purchases were carried through to completion on March 31, 1929, and in accordance with the scheme which had been decided upon the old company was put into liquidation by resolutions of April 20 and May 6, 1929. During the year ended March 31, 1929, the actual profit earned by the company was some £ 371,000. During that year the company had continued to expand, and during that year £ 220,043 had been spent on fixed assets, £ 306,960 had been spent in increasing the stock, the book debts and cash had increased by £ 103,475, and the loans to Mr. Burton had increased by nearly £ 54,000.

In addition it appears that since 1927 the system of buying premises by Mr. Burton with money advanced by the company had been altered. Two new companies had been formed known as Henry Holding, Ltd., and Key Estates, Ltd., Mr. Burton holding all the shares in Henry Holding, Ltd., and Henry Holding, Ltd., owning all the shares in Key Estates, Ltd. The system of acquiring premises had been modified so that during those two years the respondent company lent the money necessary for the purchase of the premises to Henry Holding, Ltd., who apparently

financed Key Estates, Ltd., so that that company could become the owner of the shop in which the business was to be carried on.

In those circumstances the commissioners of income tax have reached the conclusion that the company's business had been so carried on as to bring it within the purview of Section 21 of the Finance Act, 1922. It is admitted that the company is a company to which the provisions of that statute are applicable, that is to say, that it answers the definition of sub-section 6 of that section in that substantially the whole capital and control of the company were vested at all material times in Mr. Burton, now Sir Montague Burton.

By Section 21 it is provided: "With a view to preventing the avoidance of the payment of super-tax through the withholding from distribution of income of a company which would otherwise be distributed, it is hereby enacted as follows: (1) Where it appears to the special commissioners that any company to which this section applies has not, within a reasonable time after the end of any year or other period ending on any date subsequent to the fifth day of April, nineteen hundred and twenty-two, for which accounts have been made up, distributed to its members in such manner as to render the amount distributed liable to be included in the statements to be made by the members of the company of their total income for the purposes of super-tax, a reasonable part of its actual income from all sources for the said year or other period, the commissioners may, by notice in writing to the company, direct that for the purposes of assessment to super-tax the said income of the company shall, for the year or other period specified in the notice, be deemed to be the income of the members, and the amount thereof shall be apportioned among the members: Provided that, in determining whether any company has or has not distributed a reasonable part of its income as aforesaid, the commissioners shall have regard not only to the current requirements of the company's business, but also to such other requirements as may be necessary or advisable for the maintenance and development of that business." Then there are other provisions with which we are not concerned as to the distribution of the burden thus imposed.

Pusuant to that section the commissioners of income tax have determined that this company had not distributed "a rea-

sonable part of its actual income" for the year ended March 31, 1929. There seems in the Case to be some little confusion between the date and the date of February 27, 1929, when the agreement for sale was entered into; but the point is irrelevant for the matter which your Lordships are now considering.

From that decision of the commissioners of income tax there was an appeal to the special commissioners. They affirmed their direction. There was then an appeal to the Board of Referees, who confirmed the decision of the commissioners, and, as I stated at the beginning of this opinion, the only question which is open to the determination of the Court, as found in the Case stated by the Board of Referees, is whether there was evidence upon which the Board of Referees could reach that conclusion.

It is argued on behalf of the appellants that inasmuch as the whole of the sums which were earned by the company, or a sum at least as large as the whole of the sums earned by the company, in any year were expended in the maintenance or development of the business, the section is not applicable. Reliance is placed upon the findings of fact in the Case stated. The particular findings which are relied upon are to be found in sub-paragraph (xvii) of paragraph 4 of the Case stated: During the year ended the 31st March, 1929, the company expended on the current requirements of its business and on other requirements advisable for the maintenance and development of that business, amounts far in excess of the profits of the year", and then figures are set out which support that conclusion.

Counsel for the appellants took the point that on its true construction the statute meant that in any case in which the commissioners found that sums equal to the total income of the company for any year had in fact been spent on requirements necessary or advisable for the maintenance and development of the business of company, then the section did not operate. I do not so understand the section. As I read the section, the direction in the proviso is that one of the relevant factors to which attention must be paid by the commissioners and by the Board of Referees is the fact that the income, or sums equivalent to the income, have been spent on requirements necessary or advisable for the maintenance and development of the business; but I do not read the proviso as meaning that wherever that happens

then, whatever the facts are, the commissioners are bound to hold that the requirements of Section 21 have not been complied with.

In the present case it is obvious that if the company had so desired it could have paid by way of dividend the sums which in fact it lent to Mr. Burton—as he then was—and the only differences which would have been occasioned by that course of business would have been, first of all, that the company would not have been entitled to receive interest on the money so paid, and secondly that if the money had been paid by way of dividend there would have been a super-tax liability on Sir Montague Burton, and the amount of the dividend which would have been available in his hands to buy new premises would have been correspondingly diminished. But I cannot think that the fact that the company chose to carry on its business in that particular way is one which can be disregarded, or which compels the Board of Referees to reach the conclusion for which the appellant company contends.

There is also in the present case a point which is very well put, if I may say so, in the judgment delivered by Romer, L. J., in the Court of Appeal. At the end of the year ended March 31, 1929, the position was that the company had sold its whole business to the new company: it required no sums for the maintenance or development of the business which it had so transferred; it had an available asset of £ 1,000,000 in a debt owing from Mr. Burton; and there was no reason—at any rate no reason which seems in any way conclusive—why it should not have declared a dividend, which admittedly it could legally have done, and satisfied the dividend of course by writing off a corresponding proportion of the debt owing to it by Sir Montague Burton.

I began my opinion by pointing out that the only question to be determined was whether there was evidence on which the Board of Referees could have reached the conclusion which they did reach. It there were such evidence, than it is not open to this House to review their findings of fact: and in my judgment there was ample evidence. It can only be suggested that they were wrong on the basis that the proviso does not mean merely that the commissioners are to have regard to the facts

therein stated, but that they are to treat those facts as in every case conclusive, and that is a meaning which I cannot possibly put upon the language of the statute.

For these reasons I think that this appeal fails, and I move your Lordships that it be dismissed.

LORD BLANESBURGH.—I am of the same opinion.

LORD RUSSELL OF KILLOWEN.—I also agree that this appeal fails, and I am content to rely upon the judgment of ROMER, L.J., in the Court of Appeal as expressing the reasoning upon which my opinion is founded.

LORD MACMILLAN.—I also agree.

LORD ROCHE.—I agree.

Appeal dismissed.

[IN THE KING'S BENCH DIVISION.]

PETERBOROUGH ROYAL FOXHOUND SHOW SOCIETY

v.

INLAND REVENUE COMMISSIONERS.

LAWRENCE, J.

March 31, 1936.

INCOME TAX—EXEMPTION—CHARITY—AGRICULTURAL SOCIETY—MEANING OF LIVE STOCK—SOCIETY FOR PROMOTION OF FOXHOUND BREEDING—INCOME TAX ACT, 1918 (8 & 9 GEO. 5. c. 40), s. 37 (1).

A society, whose object was to promote the interest of foxhound breeding, and for that purpose to hold annually a foxhound show, claimed exemption from income tax under Schedule D, on the ground that it was a charity, or, alternatively, exemption under that Schedule on the profits arising from its show, on the ground that it was an "agricultural society" within the meaning of Section 23 of the Finance Act, 1924. That section exempts from

tax the profits of an agricultural society derived from any exhibition or show held for the purposes of the society, and defines "agricultural society" as meaning any society established for the purpose (inter alia) of promoting the interests of live-stock breeding: Held, *first, that the society was not a charity; but, secondly, that it was such an agricultural society, since the expression "live stock" includes foxhounds. It was therefore entitled to exemption from income-tax on the profits earned by its annual foxhound show.*

Cases referred to:

COMMISSIONERS FOR SPECIAL PURPOSES OF INCOME TAX *v.* PEMSEL [1891] (61 L. J. Q. B. 205; [1891] A. C. 531; 8 Tax Cas. 53).

GENERAL MEDICAL COUNCIL *v.* INLAND REVENUE COMMISSIONERS [1928] (97 L.J.Q.B. 578; 13 Tax Cas. 819).

INLAND REVENUE COMMISSIONERS *v.* YORKSHIRE AGRICULTURAL SOCIETY [1927] (97 L.J.K.B. 100; [1928] 1 K.B. 611; 13 Tax Cas. 58).

MACDUFF, *In re*; MACDUFF *v.* MACDUFF [1897] (65 L.J. Ch. 700; [1896] 2 Ch. 451).

NOTTAGE, *In re*; JONES *v.* PALMER [1895] (64 L.J. Ch. 695; [1895] 2 Ch. 649).

TETLEY, *In re*; ATT-GEN. *v.* NATIONAL PROVINCIAL AND UNION BANK OF ENGLAND [1923] (93 L.J. Ch. 231; [1924] A.C. 262).

Appeal by Case stated from a decision of the Special Commissioners of Income Tax.

The appellants appealed against assessments to income-tax under Schedule D for the year 1934-1935 in respect of their profits, and interest on their investments, on the ground that they were a charity and therefore exempt from income-tax under Section 37 of the Income Tax Act, 1918, and under Section 30 of the Finance Act, 1921, as amended by Section 24 of the Finance Act, 1927.

In the alternative the appellants claimed exemption in respect of profits arising from their annual foxhound show, on the ground that they were an agricultural society within the meaning of Section 23 of the Finance Act, 1924.

The object of the appellants was to promote the interests of

foxhound breeding in the United Kingdom and for that purpose to hold annually a foxhound show at Peterborough, open to hounds from any recognised pack in Great Britain or Ireland. At that show various prizes are awarded.

The land upon which the show is held adjoins that of the Peterborough Agricultural Society, and such land is owned by trustees, who hold it on behalf of the appellants. The show is held within the same boundaries as the Peterborough agricultural show, but the Peterborough Agricultural Society and the appellants are separate entities, and the foxhound show is held in a separate building and a separate entrance fee is charged.

The whole of the funds and income of the appellants, including the net proceeds arising from the show, are applied solely towards the promotion of the purposes of the appellants, and upon a winding-up of the appellants the surplus assets are to be applied to such charitable purposes as the committee shall by resolution appoint.

The appellants do not seek to make a profit from the show or otherwise to make a profit, but desire to cover their expenses by their receipts. If profits are made they cannot, under the present constitution, be distributed among the members. His late Majesty, King George V, was patron of the show, and by his consent it bears the title "Royal".

On behalf of the appellants it was contended, first, that the appellants were a society the sole object of which was the improvement of animals useful to mankind, and therefore that they were a charity and as such exempt from income-tax. Secondly, that they were an "agricultural society" employed in live-stock breeding within the meaning of section 23 of the Finance Act, 1924, and as such entitled to exemption from income-tax on the profits derived from the show; and, thirdly, that foxhounds were live stock, since the definition of live stock in the Finance Act, 1923, included animals of any description, and that the same definition must be applied in construing section 23 of the Finance Act, 1924.

The Crown disputed all three contentions.

The Special Commissioners held that the appellants were not a charity and were not an "agricultural society", and accordingly refused the claim for exemption.

The relevant sections of the Income Tax and Finance Acts of England run as follows :—

Income Tax Act, 1918, section 37 (1): "Exemption shall be granted . . . (*b*) . . . from tax under Schedule D in respect of any yearly interest or other annual payment forming part of the income of any body of persons or trust established for charitable purposes only . . . "

Finance Act, 1921, section 30 (1) (see section 24 of the Finance Act, 1927): "Exemption shall be granted . . . (*c*) from income-tax under Schedule D in respect of the profits of a trade carried on by any charity, if the profits are applied solely to the purposes of the charity and either (i) the trade is exercised in the course of the actual carrying out of a primary purpose of the charity; or (ii) the work in connection with the trade is mainly carried on by beneficiaries of the charity."

Finance Act, 1923, section 11 (2): "In this section . . . the expression 'live-stock' includes animal of any description."

Finance Act, 1924, section 23 (2): "Any profits or gains arising to an agricultural society from an exhibition or show held for the purposes of the society shall, if they are applied solely to the purposes of the society, be exempt from income-tax."

(2) "The expression 'agricultural society' in this section means any society or institution established for the purpose of promoting the interests of agriculture, horticulture, live-stock breeding or forestry."

J. M. Tucker, K. C., and *Walker Carter*, for the appellants.

The Attorney-General (*Sir Donald Somervell, K.C.*), and *R. P. Hills*, for the respondents.

JUDGMENT.

LAWRENCE, J.—The first question I have to decide is whether the appellant society is exempt from income-tax on the profits of its show by reason of section 23 of the Finance Act, 1924, which provides that profits arising to an agricultural society from a show held for the purposes of the society shall, if they are applied solely to the purposes of the society, be exempt from income-tax, and defines an agricultural society as one established for the purpose of promoting the interests of agriculture, horticulture, live-stock breeding or forestry.

By its constitution, the purpose of the appellant society is to

promote the interests of foxhound breeding, and the only question on this branch of the appeal is whether foxhound breeding is live-stock breeding within the meaning of Section 26 of the Finance Act, 1924. In my opinion, it is. The words "live stock" are ordinarily and properly used in contrast with dead stock and include all live animals and birds the breeding of which is regulated by man. In *Murray's*, the only dictionary to which my attention was called, the words are defined as "domestic animals or animals kept for use or profit". They are defined in the Finance Act, 1923, s. 11, for the purpose of exempting live-stock shows from entertainment duty, as including animals of any description, and they are used in a somewhat similar sense in the Agricultural Holdings Act, 1923, s. 12 (6), ss. 34 to 36, and s. 57.

It was contended for the Crown that the words ought to be construed, in view of their context, in accordance with the maxim *noscitur sociis* as referring only to animals whose use is an integral part in agriculture, horticulture, or forestry. But such an interpretation would exclude many animals which are bred in the ordinary course of agriculture and shown throughout the country; for example, town and van horses, hackneys, hunters, racehorses, most breeds of dogs, and fur-bearing animals. I see no reason why the words should receive this limited interpretation, particularly as it was the will of the Legislature that such societies should be exempted from entertainments duty.

The second question is whether the appellant society is exempted from income-tax under Section 37 of the Finance Act, 1918, on the ground that it is established for charitable purposes only. It was contended for the Crown, though but faintly, that the question is one of fact, and that the Commissioners' finding is binding upon me; but as I read the decisions upon this subject, it is for the Commissioners to say what are the purposes of the society, and for the Court to decide as a matter of law whether those purposes are charitable. The only finding of fact as to the object of this society is in paragraph 3 of the Case, namely, that it is to promote the interests of foxhound breeding.

The appellants seek to bring their society within the fourth category stated by Lord Macnaghten in *Commissioners for Special purposes of Income Tax* v. *Pemsel*, on the ground

inter alia, that foxhunting is good for the community at large because it keeps money in the country and brings it into the countryside, and also good for officers in the army and those who take part in it, and that it makes for the well-being of animals, which is for the benefit of the community.

Though I am firmly convinced of the truth of these propositions of fact, I am unable to take the view that the appellant society is established for charitable purposes only. It has, I think, been authoritatively laid down that Lord Macnaghten's fourth category must be tested by reference to the subjects mentioned in the Statute of Elizabeth itself—see *Macduff, In re*; *Macduff* v. *Macduff* (65 L. J. Ch., at p. 704; [1896] 2 Ch., at p. 467). Adopting this method of interpretation, I can see no satisfactory analogy between a foxhound society and the matters referred to in the Statute of Elizabeth. The difficulty in this class of case arises principally from the mixture of motives or purposes which appears to exist in the minds of founders of such societies. A society may be established with an immediate direct but incidental motive or purposes which is not charitable; for example, to promote the sports of a particular regiment, but with an ultimate indirect but main purpose which is charitable, and in that case it comes within the exemption—see *Nottage*, In re; *Jones* v. *Palmer* (64 L.J. Ch., at p. 701; [1895] 2 Ch., at p. 656 *per* Rowlatt, J., in *Inland Revenue Commissioners* v. *Yorkshire Agricultural Society* (13 Tax Cas., at p. 66) and *per* Atkin, L.J. (97 L.J.K.B., at p. 108; 13 Tax Cas., at p. 77) and *per* Sargant, L.J., *General Medical Council* v. *Inland Revenue Commissioners* (97 L.J.K.B. at p. 587; 13 Tax Cas. at p. 849); and per Lord Haldane in *Tetley*, In re; *Att.-Gen.* v. *National Provincial and Union Bank of England* (93 L.J. Ch., at p. 234; [1924] A.C, at p. 267). Similarly, in *Inland Revenue Commissioners* v. *Yorkshire Agricultural Society*, the benefit of members and, as I think, the hound show were incidental purposes, agriculture being the main purpose.

The question then, in my opinion, is whether the society's main or dominant purpose is charitable. In the present case I am of opinion that the main purpose of the appellant society's activities is to benefit foxhunting, not to benefit the community.

The case most favourable to the appellants' contention is

Inland Revenue Commissioners v. *Yorkshire Agricultural Society*. There agriculture was held to be the main purpose of the society and was considered to be directly beneficial to the community, whereas here foxhunting cannot, in my opinion, be said to be directly beneficial to the community. At any rate, foxhunting is not in my opinion, analogous to the subjects mentioned in the Statute of Elizabeth, and I therefore hold that the appellant society is not established for charitable purposes only.

The appeal will be allowed in part with reference to the live-stock breeding point.

Appeal allowed in part.

[NOTE :—The fourth category stated by LORD MACNAGHTEN and referred to in the Judgment is 'trusts for other purposes beneficial to the community not falling under any of the preceding heads'; and the preceding heads are trusts for relief of poverty; trusts for the advancement of education; trusts for the advancement of religion.—*Ed.*].

[IN THE COURT OF APPEAL.]

McKENNA (INSPECTOR OF TAXES) *v.* EATON-TURNER.

LORD HANWORTH, M. R., ROMER, L.J., MAUGHAM, L. J.

July 3, 4, 5, 1936.

REVENUE—INCOME TAX—TAXPAYER RESIDENT IN ENGLAND —EMPLOYMENT PARTIALLY ABROAD—LIABILITY IN RESPECT OF SALARY—INCOME TAX ACT, 1918 (8 & 9 GEO. 5 c. 40), s. 1, SCHED. D, PARA. 1 (*a*) (*ii*); SCHED. E, RULES APPLICABLE TO SCHED. E, R.6—FINANCE ACT, 1922 (12 & 13 GEO. 5, c. 17), s. 18.

A person resident in England, but employed in West Africa by an English company controlling their business from England is chargeable with income tax under Schedule E in respect of the emoluments of his employment, which were paid to him for the most part in England, the facts falling within Case II of

Schedule D, transferred to Schedule E by Section 18 of the Finance Act, 1922.

COLQUHOUN *v.* BROOKS [1889] (59 L.J.Q.B. 53; 14 App. Cas. 493; 2 Tax Cas. 490) *explained and distinguished.*

FOULSHAM *v.* PICKLES [1925] (94 L.J.K.B. 418; [1925] A.C. 458; 9 Tax Cas. 261) *followed.*

Decision of SINGLETON, J. (104 L.J.K.B. 190; [1935] (1 K.B. 466) *affirmed.*

Cases referred to:

COLQUHOUN *v.* BROOKS [1889] (59 L.J.Q.B. 53; 14 App. Cas. 493; 2 Tax Cas. 490).

FOULSHAM *v.* PICKLES [1925] (94 L.J.K.B. 418; [1925] A.C. 458; 9 Tax Cas. 261).

LONDON BANK OF MEXICO AND SOUTH AMERICA *v.* APTHORPE [1891] (60 L.J.Q.B. 653; [1891] 2 Q.B. 378; 3 Tax Cas. 143).

SAN PAULO (BRAZILIAN) RAILWAY *v.* CARTER [1895] (64 L.J. Q.B. 379; [1895] 1 Q.B. 580; 3 Tax Cas. 344; affirmed in H.L., 65 L.J.Q.B. 161; [1896] A.C. 31; 3 Tax Cas. 407).

Appeal of the taxpayer from the decision of Singleton, J., on a Case stated by the Commissioners for the Special Purposes of the Income Tax Acts.

The assessments against which the appeal was made were imposed under Schedule E in respect of the emoluments of employment by the Ashanti Goldfields Corporation, Ltd., a company which carries on the business of gold mining in West Africa, and has a registered office in London. The emoluments consisted of an annual salary while the appellant was at the mines, payments for time on voyages to and from West Africa, holiday pay for two months at the end of each tour, and a visitors' entertainment allowance, the last-mentioned item being payable at the mines, though the main parts of the salary were payable in England. The assessments related to the years 1926-7 to 1933-4, that for the first year being made in duplicate under Schedule D and Schedule E. The case was argued on the footing that the assessment applicable for that year was that under Schedule E, by reason of the transfer to the latter schedule by Section 18 of the Finance Act, 1922. It was admitted that the appellant was resident in England, where he had a wife and children, for all the

period in question after June 11, 1926, and the Commissioners found upon evidence that he was so resident even before that date. He satisfied the commissioners that until the making of an agreement in September, 1932, all his duties were performed in West Africa, and the commissioners decided that he did not fall within the charge of Case II of Schedule D until the making of that agreement.

Singleton, J., on an appeal of the Crown, held that the commissioners were wrong, and the taxpayer appealed.

Needham, K.C., and *Cyril King*, for the appellant.

The Solicitor-General (*Sir D. B. Somervell, K.C.*) and *R.P. Hills*, for the Crown.

LORD HANWORTH, M.R.—This is an appeal from a judgment of Singleton, J., and the question which has to be determined is whether or not the subject, the appellant, Mr. Eaton-Turner, is liable to suffer taxation in accordance with certain assessments which have been made upon him.

The appellant was assessed for 1926-27 and for the subsequent years down to the year 1933-34 at a sum of £ 2,500. That sum represents the salary and commission paid to him in respect of services rendered to a company called the Ashanti Goldfields Corporation, Ltd. The company was incorporated under the Companies Act on May 25,1897, and carries on a gold-mining business in West Africa. Its registered office is situate in London, but the active part of the appellant's services to the company is carried out in West Africa.

The appellant was absent from England and engaged in the activities of his work in West Africa during a very considerable period of the year, but it was admitted that he was resident in the United Kingdom, where he has a wife and children and a house. There was some dispute on the question whether in respect of one year he was resident, but upon the facts before them, the commissioners held that he was resident in the United Kingdom. The result is that he is to be treated as resident in the Kingdom during all these years of assessment. Although his actual activities in his capacity as (I think) a manager were performed abroad he was paid over here. The Case finds that the commissioners "were satisfied that before the agreement of September 2, 1932, no part of the respondent's work or duties

fell to be performed or was performed in the United Kingdom." But the Case shows that he was, in the main, paid by remittance to England, either through the Westminster Bank, or through the Bank of New Zealand. Lord Cave, L. C., when he was dealing with the case, which is by no means dissimilar, of *Foulsham (Inspector of Taxes)* v. *Pickles* (94 L. J. K. B., at p. 420; [1925] A. C., at p. 463; 9 Tax Cas., at p. 287), said: "In other words while the burdens incidental to his employment were to be borne wholly or mainly abroad, the principal benefit which he was to derive from it could only be claimed in the United Kingdom."

It is now contended on behalf of the appellant that he is not liable to be assessed at all in respect of any portion of these sums which are included in the assessments. The grounds on which that argument is put forth are that he is not chargeable under Schedule E, for reasons with which I will deal later, and primarily: "that the whole of his duties under these agreements were in fact performed on the company's property abroad and that the office of the appellant was not an office or employment of profit within the United Kingdom for any of the years of assessment." The real basis for that argument is the decision of the House of Lords in the case of *Colquhoun* v. *Brooks*. It is important to remember that that case was decided under what I may call comprehensively the old income tax law before it had been embodied, and to a large extent consolidated, in the Income Tax Act, 1918. Mr. Brooks was a man who resided wholly in England; he was also a partner in a firm carrying on business solely in Melbourne, Australia. Large profits were made by the firm and a portion of his share of the profits was remitted to him in England. That portion was duly returned by him for assessment under Schedule D, but the larger portion of his share of profits in the firm was left in Australia, and never at any time formed part of his income in this country. The two businesses —that is, the business which he carried on in England and that which was carried on in Melbourne, Australia—were entirely distinct. Mr. Brooks returned as assessable a sum of £3,000, which represented the entire sum remitted to him from his Australian firm during the financial year in question. But there was standing to his credit in the books of the Australian firm at

Melbourne a sum of £9,219, which was a profit realised and capable of being remitted; that is to say, it was an ascertained profit. No portion of this £9,219 had been received in England; it remained entirely in the hands of the firm in which he was a partner. The surveyor of taxes contended that Mr. Brooks ought to be assessed not only on the sum of £3,000 which had been remitted from Australia, but also upon the sum of £9,219 which lay in the hands of his Australian firm in Melbourne. That assessment having been made upon him, the commissioners on an appeal formed the opinion that the assessment ought to be confined to such sums as were from time to time received by Mr. Brooks in Great Britain; and they allowed his appeal against the assessment and reduced its amount by deducting from the assessment the sum of £9,219 which was the amount in controversy.

When the matter came before the Divisional Court, as revenue cases did in those days, there was a difference of opinion. Stephen, J., held that the wide words of Schedule D embraced an item like the £9,219, and therefore that the subject was liable to tax in respect of it; Wills, J., differed. It is interesting to see why Stephen, J., held that there was a liability, and it is simply and broadly for the reason that Schedule D of the Income Tax Act, 1842, imposed the tax in respect of the "annual profits and gains arising or accruing to any person residing in Great Britain, from any . . . trade . . . whether the same shall be . . . carried on in Great Britain or elsewhere." Those wide words are in Schedule D of the Income Tax Act, 1918, where it is provided as follows in para. 1: "Tax under this schedule shall be charged in respect of—(a) The annual profits or gains arising or accruing . . . (ii) to any person residing in the United Kingdom from any trade, profession, employment, or vocation, whether the same be respectively carried on in the United Kingdom or elsewhere;". Stephen, J., was of opinion that those wide words were wide enough to embrace this sum of £9,219 lying at the disposal of the subject at Melbourne. Wills, J., took a different view, but, following the practice of those days, in accordance with the old practice of the Court of Exchequer, Wills, J., withdrew his judgment, and judgment was given for the Crown. Mr. Brooks appealed, and the Court of Appeal held

that he was not liable. They held that although those very wide words would embrace this contested item, yet the words were not to be taken in the full significance of their terms. Fry, L.J., dissented. The House of Lords affirmed the judgment of the Court of Appeal, holding that Mr. Brooks was not liable, but stating that their reasons differed somewhat from those of the Court of Appeal. It is not quite easy to understand what the divergence was.

I turn to *Colquhoun* v. *Brooks* as reported when it was before the House of Lords. It must be remembered that there were in the Act of 1842 a number of what are called Cases, just as there are in that of 1918. The First Case related to the duties to be charged in respect of a trade, manufacture, adventure or concern. The Second Case related to duty to be charged in respect of professions, employments or vocations. The Fourth Case related to income out of the United Kingdom arising from securities, and the Fifth Case related to income from possessions out of the United Kingdom. The argument which was presented was that the terms of the statute of 1842, having declared that the tax imposed by Schedule D was to be charged under six Cases, one or other of those Cases must fit the tax if it was to be exigible under Schedule D. Two Cases were relied upon in *Colquhoun* v. *Brooks*. The Court was there dealing with a trader carrying on business, and so the first Case referred to was Case I: "Tax in respect of any trade . . ." But Case V dealt with income arising from possessions out of the United Kingdom and it was said: "It is all very well to suppose that Case I applies, because that covers a trade, whether it be carried on in the United Kingdom or elsewhere; there is another Case which is more appropriate to the facts, and if so, division which is indicated in these Cases ought to be adhered to and the Case ought to be applied which is most appropriate to the facts." And it is pointed out by Lord Herschell (59 L.J.Q.B., at p. 58; 14 App. Cas., at p. 504; 2 Tax Cas., at p. 499) that Case IV deals with income from securities out of the United Kingdom but only makes chargeable such sum as has been received in the United Kingdom. Equally Case V deals with income arising from possessions outside the United Kingdom, but the tax falls only on so much of the income as is received in this country, whereas, if the income

were dealt with under Case I, the whole is subject to taxation, although no part of it ever reaches this country.

Is it possible to assume that that was the intention of the Act? The argument was put in this way by Lord Herschell (59 L.J.Q.B., at p. 59; 14 App. Cas., at p. 506; 2 Tax Cas., at p. 500): "It is said that although elaborate machinery is provided for carrying out the taxing purposes of the Act, none of it is applicable to the assessment of the profits of a trade carried on entirely outside the United Kingdom and no part of which is received here. If this be correct, it certainly goes far to show that the Legislature cannot have intended to tax such profits." He then goes into the discussion germane to that problem. Lord Macnaghten said (59 L.J.Q.B., at p. 62; 14 App. Cas., at pp. 511-512; 2 Tax Cas., at pp. 504-505): "The question after all really lies in a narrow compass. Does the case fall within the 'First Case' of Schedule D in the Income Tax Act of 1842, and under the head of 'Duties to be charged in respect of any trade, manufacture, adventure, or concern in the nature of trade, not contained in any other schedule of this Act'; or does it fall within the 'Fifth Case' under the head of 'The duty to be charged in respect of possessions in Ireland, or in the British Plantations in America, or in any other of Her Majesty's dominions out of Great Britain, and foreign possession'? Or, to put the question more shortly still, what is the meaning of the term 'possessions' in the 'Fifth Case' of Schedule D and in other places in the Act where it is used in the same connection?" And Lord Macnaghten said further (59 L.J.Q.B., at p. 64; 14 App. Cas., at p. 514; 2 Tax Cas. at p. 507): "The income of the respondent from his business in Melbourne, whether he is to be charged in accordance with the connection of the Attorney-General or not, undoubtedly comes under Schedule D. Undoubtedly, the portion of Schedule D which is contained in Section 1 of the Act of 1842 is expressed in the most comprehensive terms possible, and if not restrained or limited by what follows, would operate to charge the respondent in respect of the whole of his Melbourne income. I do not, however, agree with the argument urged at the Bar, that the rest of Schedule D, which is found in Section 100, is mere machinery, or a mere collection of examples, not diminishing the generality of the earlier part of the schedule,

but intended only to furnish a guide where the particular rule applies." Further on, he said (59 L. J. Q. B., at p. 64; 14 App. Cas., at p. 515; 2 Tax Cas., at p. 507): "unquestionably the rules applicable to a particular 'Case' may cut down and cut down very materially, the charging words in the earlier part of Schedule D"; and again (59 L. J. Q. B., at pp. 64, 65; 14 App. Cas., at p. 516; 2 Tax Cas., at p. 508): "there are other provisions which it is not necessary to go through, which seem to show that the 'First Case', though clearly applying to a trade carried on partly abroad and partly in Great Britain, was not intended to apply to a trade carried on exclusively abroad." He then turns to the Fifth Case and asks what is the meaning of "possessions" and he comes to the conclusion that the business carried on abroad was within the ambit of the word "possessions." The result was that he holds that the Fifth Case was more appropriate than the First Case, for upon the facts the trade was carried on exclusively abroad. If so, it was not at the volition of the Crown to tax the subject under Case I, because there was another Case, Case V, which fitted the case and, as it fitted the case and controlled the large embracing words at the beginning of Schedule D, it limited the chargeability to tax. He held that the sum of £9,219 was a profit derived from a possession abroad within the Fifth Case and that under that case the only amount of profits that could be made chargeable to tax was the sum remitted. The tax upon that amount had already been paid, and nothing therefore remained chargeable in respect of that sum. *Colquhoun* v. *Brooks* does, therefore, establish that it must be seen which Case is appropriate to the facts in question, and if the Fifth Case is appropriate it cannot be put into force to charge more than the profits actually received at home. The decision is important, as showing that the initial general words of Schedule D may be cut down by a later portion, because it is clearly indicated that those general words are to be made effective through the Cases which are more precise in their language, have certain rules applicable to them, and provide the channel through which the chargeability is to reach the subject. And if along one or other of those channels chargeability cannot be imposed, then to that extent the wide and general words with which Schedule D opens are to be treated as cut down.

That is the effect of *Colquhoun* v. *Brooks*. We are not without some guidance as to the effect of that case. Let me turn to the next case, in which it was first of all discussed, *London Bank of Mexico and South America, Ltd.* v. *Apthorpe*, a case decided in the Court of Appeal. In that case Lord Esher, M. R., came to the conclusion that there was really little, if any, divergence between the Court of Appeal and the House of Lords in *Colquhoun* v. *Brooks*, and he said (60 L. J. Q. B., at p. 655; [1891] 2 Q. B., at p. 382; 3 Tax Cas., at p. 147): "Where a person carries on two businesses—one which is carried on in England in the ordinary sense of the words, and another wholly distinct business which is carried on abroad—then you cannot join the two businesses, and charge him in respect of them, together. You must deal with the one in England only as a business carried on in England, and with the other as a business carried on solely abroad, and assess him in respect of each accordingly. As to the business carried on abroad, he can only be assessed in respect of so much money as he gets out of that business, and as comes into his hands in England. That is the result of the decision in *Colquhoun* v. *Brooks*."

Colquhoun v. *Brooks* was once more discussed in the case of *San Paulo (Brazilian) Railway* v. *Carter*. There Rigby, L. J., was discussing the effect of *Colquhoun* v. *Brooks*, and he said (64 L. J. Q. B., at p. 384; [1895] 1 Q. B., at p. 588; 3 Tax Cas., at pp. 353, 354): "The House of Lords went, it appears from the report, into a more minute examination of the sections of the Income Tax Acts than was made in this Court. The mode in which they arrived at the conclusion which they adopted was as follows: they seem to have been of opinion that, although the facts of the case came within the general words of Schedule D and the First Case, yet such general words might be cut down in some cases by other parts of the Act; and, not finding upon examination of the sections of the Act any means of assessing the profits of a trade or business, unless it was at any rate partly carried on in the United Kingdom, they thought themselves justified, notwithstanding the general words used, in limiting the operation of the First Case to cases where the Act provides means of assessment; and then they considered the case of a business entirely carried on abroad as one coming within the

Fifth Case, under which persons receiving profits from 'foreign possessions' are assessable on such profits as they actually receive in this country." That is statement of the effect of *Colquhoun* v. *Books*. The appropriate Case has to be ascertained, and if an appropriate Case is found it cannot be discarded and another Case used because it will give the Crown a better result in charging the subject. When the *San Paulo Case* came before the House of Lords, Lord Watson said (65 L.J.Q.B., at p. 164; [1896] A.C., at p. 40; 3 Tax Cas. at p. 411): "When it has been ascertained that a person interested in the profits of a trade has his residence in the United Kingdom, in such sense as to bring him within the incidence of the Income Tax Acts, the only question remaining for consideration is whether the measure of his liability is to be found in the First or in the Fifth Case of Schedule D; in the one case, he is liable to pay duty in respect of the net profits accruing to him from such trade; in the other, in respect only of such part of these profits as shall have been actually received by him in this country. But he cannot, according to the rule established in *Colquhoun* v. *Brooks*, escape from liability under the First Case, unless he is able to show that no part of the trade is carried on within the United Kingdom, or, what comes to precisely the same thing, that the trade is exclusively carried on in a country or countries outside the United Kingdom, whether subject to Her Majesty or not. If he succeeds in proving that fact, his liability will be under the Fifth Case."

It does not therefore follow from *Colquhoun* v. *Brooks* that there may not be a liability in respect of a business the activities of which are carried on abroad; it has to be shown that the trade, or the employment—because we are dealing with Case II, which deals with employment and not trade—is exclusively carried on in a country outside the United Kingdom.

Here we have to consider the case of a man whose duties are exercised outside the United Kingdom. But does that cover the whole of the contract under which his service was rendered? I think one must consider the case of *Foulsham* v. *Pickles*, and bear in mind the comments that were made upon that case which is admittedly very like the present one. Lord Cave used

the words to which I have already referred. Lord Dunedin said (94 L.J.K.B., at p. 421; [1925] A.C., at p. 466; 9 Tax Cas., at p. 289); "When I say made in the United Kingdom I am not referring to the place where the signing of the contract took place. I am referring to the source of the profit which is the payment which the employers covenanted to make. This was payable and paid in London." Lord Buckmaster said (94 L.J.K.B., at p. 422; [1925] A.C., at p. 467; 9 Tax Cas., at p. 290): "He was engaged by the African Association, Ltd., to serve them in West Africa as district supervising agent at a salary of £500 and commission, and by the terms of his employment it was provided that he should not draw nor claim payment in the colony in respect of commission, but payment thereof should only be made to him through the office of the company in Liverpool", and they held upon the facts of that case that it was not one in which there was exclusive employment abroad, and that, having regard to the mode of payment provided by the contract, the respondent's employment was not wholly out of the United Kingdom, and was not, therefore, a possession within Case V. Inasmuch as in that case the assessment had been imposed upon the subject under Case V, and only under Case V, the House of Lords agreed with the Court of Appeal in not allowing the matter to be remitted for a different Case to be made applicable, such as Case II.

Having examined those cases very carefully, I have come to the conclusion that the facts of the present case are similar to those in *Foulsham* v. *Pickles*, and that it is not established upon the facts found by the Commissioners that this employment is one wholly abroad. It is not, therefore, a case which falls within Case V. I think in loyalty to *Foulsham* v. *Pickles* we must come to that conclusion; but independently, I have arrived at the same conclusion. Case II provides that tax can be collected in respect of any profession or employment. It has been suggested that some limitation ought to be imposed upon the words of Case II by reason of the rules, but I do not find any grounds for saying that the ambit of Case II is so reduced, and it seems, therefore, that the general words of Schedule D apply to the case, that Case II is the particular Case applicable, Case V does not apply, and therefore the authority of *Colquhoun* v. *Brooks*

cannot be invoked to render the appellant immune from these assessments.

A subsidiary point was made, which was based upon the terms of Section 18 of the Finance Act, 1922, which brought certain cases which hitherto fell to be charged under Schedule D back to chargeability under Schedule E. The first proposition of the appellant's counsel was that their client was not chargeable under Schedule D and therefore was not brought back into charge under Schedule E. I have dealt with that point. Then it is said that, although he is brought back into charge under Schedule E, yet regard must be had to the rules applicable to Schedule E, and since you find rule 6, which provides that, "The tax shall be paid in respect of all the public offices and employments of profit within the United Kingdom, . . . " it follows that once more the effect of the section is cut down by the rules. That argument does not appeal to me. It is stated in the very terms of Section 18 (1) that the rules applicable to Schedule E are to "apply accordingly subject to the provisions of this Act". I cannot so interpret the rules as withdrawing from the effect of Section 18 and Schedule E the very cases which it was the purpose of Section 18 to make chargeable under Schedule E.

For these reasons I am of opinion that the appeal fails and must be dismissed with costs.

ROMER, L.J.—The first question arising upon this appeal is whether before the coming into operation of the Finance Act, 1922, the appellant was chargeable in respect of the profits of his employment under Schedule D. For the purposes of this judgment I shall assume that the appellant exercised his employment wholly abroad. On that assumption I turn to Schedule D and I find that under clause 1 of that Schedule tax under it "shall be charged in respect of" (I am only going to read the portions that are material for the present purpose) "(*a*) the annual profits or gains arising or accruing—(ii) to any person residing in the United Kingdom from any . . . employment . . . whether the same be respectively carried on in the United Kingdom or elsewhere". Clause 2 provides that: "Tax under this Schedule shall be charged under the following Cases respectively; that is to say . . . Case II—Tax in respect of any profession, employment, or vocation not contained in any other Schedule".

Pausing there it would seem plain that the appellant is chargeable in respect of profits derived by him from his employment out of the United Kingdom. But it is said for him that we cannot hold that he would have been chargeable under Case II of Schedule D without entirely disregarding the reasons that were given by the members of the House of Lords in their decision in *Colquhoun* v. *Brooks.* In that case the Court was not dealing with a case of employment; it was dealing with a case of trade, and what the Court had to decide was whether Mr. Brooks in respect of the trade carried on by him wholly in Australia was chargeable under Case I of clause 2 of the Schedule or under Case V. It is extraordinary unlikely that the Legislature intended that a person in the position of Mr. Brooks should be chargeable under both Case I and Case V, seeing that if he were chargeable under Case I he was chargeable in respect of the whole of his profits derived from the trade, but, if he were chargeable under Case V, he would be chargeable only in respect so much of the profits as was received in the United Kingdom; so that the House of Lords were confronted with the necessity of deciding under which of the two Cases Mr. Brooks was chargeable. It was pointed out that if one read clause 1 (*a*) (ii) of the Schedule and Case I together, and stopped there, it would seem plain that Mr. Brooks was chargeable under Case I. But the learned Lords, especially Lord Herschell and Lord Macnaghten, on looking at other parts of the Act, notably the rules relating to assessment and collection of the tax, were driven to the conclusion that the Legislature did not intend such a case as that of Mr. Brooks to come under Case I, but under Case V. Lord Macnaghten, after reading the parts of the Schedule to which I have already called attention, said (59 L. J. Q. B., at p. 64; 14 App. Cas., at p. 515; 2 Tax Cas., at pp. 507-8): "This rule points to a business carried on out of Great Britain as well as to one carried on in Great Britain. But then, when one tries to apply the rules and provisions of the Act relating to profits and gains from trades to a trade carried on exclusively abroad, one gets into hopeless difficulties. If it is a partnership business, as this is, the return is to be made by the senior partner resident in Great Britain. But then the partner is to make the return 'on behalf of himself and the other partner or partners', and his

return is sufficient authority to charge such partners jointly and 'no separate statement' is to be allowed in any case of partnership except for 'the purpose of the partners separately claiming an exemption' or 'of accounting for separate concerns'. Then again the computation of the duty to be charged in respect of any concern in the nature of trade is to be made exclusive of the profits or gains arising from lands occupied for the purpose of such concern. That rule hardly seems applicable to a foreign mine or a sugar plantation in the West Indies. Then again by Section 106 every person engaged in any trade is to be chargeable by the commissioners acting for the Parish or place where the trade is carried on, whether such trade is exercised wholly or in part only in Great Britain And there are other provisions, which it is not necessary to go through, which seem to show that the 'First Case', though clearly applying to a trade carried on partly abroad and partly in Great Britain, was not intended to apply to a trade carried on exclusively abroad."

It is said on behalf of the appellant in this case that there are provisions in this Act which show that, notwithstanding the clear words of clause 1 of Schedule D, Case II is not intended to apply to an employment exercised wholly abroad. We asked counsel in the course of his argument what other provisions in the Act ought to lead us to that conclusion and he said Section 106 of the Income Tax Act, 1842, and that was all. He said—and said truly, if I may so—that that section did not provide machinery for the collection of emoluments arising from an employment exercised wholly abroad; and he said that that is a conclusive reason for holding that Case II does not apply to such an employment. I cannot take that view. Where there is a question whether a case falls within one charging section or another, or within one Case of a charging section rather than another Case of the same charging section, it is very relevant to a solution of such a question that if the Court adopts one construction there is no means provided by the Act for the collection of the tax, whereas if the Court adopts another construction means are so provided. The matter is not conclusive; it is merely a relevant consideration, and where as here, there is no question where these emoluments are chargeable under Case V or under Case II, I am not in the least

impressed by the fact that if I hold that the case falls within Case II no machinery is provived by the Act for the collection of that tax. If the tax is clearly imposed, the omission of the Legislature to provide means for its collection must be regarded as an unfortunate omission and nothing else. It is only where a doubt arises whether the tax is chargeable by a certain section that the absence of machinery for collection becomes a relevant consideration. I should therefore have been prepared to hold that even under the Act of 1842 the appellant's earnings in respect of his employment abroad were charged by Schedule D, notwithstanding that Section 106 of that Act provided no machinery for its collection. But in point of fact we are dealing here with the Act of 1918, and in the Act of 1918, happily for the Crown in such cases, rule 4 of the miscellaneous rules applicable to Schedule D does provide machinery for the collection of the emoluments payable in respect of an employment exercised wholly abroad. As I read *Colquhoun* v. *Brooks*, it was only because the House of Lords had to decide between Case I and Case V that Section 106 provided not only a relevant but almost a conclusive reason for the decision which the House gave.

That being so, the next question which arises on the appeal is whether the appellant is now chargeable as to his salary under Schedule E or whether he is freed from all taxation on it by virtue of the provisions of the Act of 1922? It is plain that if, as I hold is the case, the appellant was chargeable under Schedule D in respect of profits arising from his employment, according to the plain words of Section 18 of the Finance Act, 1922, those profits are no longer chargeable under that schedule but are to be chargeable to tax under Schedule E. The section goes on to say "and the rules applicable to that schedule shall apply accordingly subject to the provisions of this Act". It is argued on behalf of the appellant that if one looks at rule 6 to Schedule E, it will be found that though the Act of 1922 brings such cases as that of the appellant within Schedule E, rule 6 immediately throws them out of that schedule again. Rule 6 is in these terms: "The tax shall be paid in respect of all the public offices and employments of profit within the United Kingdom." I cannot think that, the Legislature having said that such a case

as the appellant's shall be chargeable under Schedule E in future, its intention is defeated by a subsequent provision in Section 18 that "the rules applicable to that schedule shall apply accordingly subject to the provisions of this act". As was pointed out by the Solicitor-General, if the appellant's argument is to succeed on that point, rule 6 would not only throw out of Schedule E such cases as the appellant's but it would also throw out of the schedule all cases of employment which was not a public employment of profit. It would appear that rule 6 will continue to apply to such cases as those to which it was applicable before. I cannot think that the effect of the rule is to apply to such a case as the present, with the result that it is thrown out of the schedule altogether, and having been thrown out of Schedule D by the Act of 1922 is not chargeable under any schedule at all.

For these reasons I think that the learned Judge came to the right conclusion and this appeal fails.

MAUGHAM, L.J.—I am of the same opinion. I should like to state the way in which I regard the matter, so far as it relates to the first point namely the question of the assessability of the appellant under Case II, Schedule D, clause 1 (*a*) (ii) and section 18 of the Finance Act, 1922. The facts are, of course, found in the Case stated. The only facts which I think it necessary to mention are that the appellant is resident here; that he is employed by an English company with a registered office here; that the company owns a business which is controlled from here; and that the remuneration of the appellent is, for the most part, received here. There is a finding in paragraph 5 of the Case which, no doubt, has to be borne in mind, but it ought not to be misunderstood. The finding is that the commissioners "were satisfied that before the agreement of September 2, 1932"—with which we are not concerned—"no part of the respondent's" (the present appellant's) "work or duties fell to be performed or was performed in the United Kingdom". I am accepting that to the full but I would observe that if one looks at the agreement it will be found that in almost every clause there is something to show that the appellant is not unconcerned with what the board of directors here may require him to do. He has to fulfil their instructions in many respects; he owes a duty to them; he has to render reports to them. The agreement is one

which, of course, has to be construed according to English law, and in the full sense it is an English contract. In those circumstances, apart from the operation of section 18 of the Finance Act, 1922, was the appellant assessable and chargeable under Case II of Schedule D?

The first observation which I want to make is that beyond all doubt the language of Case II does extend to and relate to the appellant. Clause I of Schedule D of the Income Tax Act, 1918, refers to tax being charged on the annual profits or gains arising or accruing to any person residing in the United Kingdom—that is where the appellant resides for income-tax purposes—from any employment, whether the same be carried on in the United Kingdom or elsewhere; and when we turn to clause 2 we find that in Case II the tax under the Schedule has to be charged "in respect of any profession, employment, or vocation not contained in any other schedule". For the present purpose I am omitting Schedule E because that did not apply before the Act of 1918 came into force. So that, since the employment may be carried on in the United Kingdom or elsewhere, the words I have mentioned are clearly sufficient to include the case of such a resident as the appellant, who is employed abroad, and *a fortiori* if he is employed abroad by people residing in this country and employed under an English agreement. Then it is said that if the case of *Colquhoun* v. *Brooks* is considered it will be seen that the operation of the words to which I have referred in clause I of Schedule D of the Act of 1918, having regard to the decision of the House of Lords, must be limited or qualified in the way in which it is said that those words were limited or qualified by the House of Lords in *Colquhoun* v. *Brooks*, when the Act of 1842 was under consideration.

I am not going into any elaborate consideration of what *Colquhoun* v. *Brooks* decide, having regard to the analysis of the case which the Master of the Rolls has given. I will only observe that I think it may be said with reasonable accuracy that *Colquhoun* v. *Brooks*, which related, as we know, to a trade carried on abroad, was decided on two considerations: first, that according to the language of the Act the taxpayer was liable to be charged under Case V in respect of income arising from a possession out of the United Kingdom, and secondly that there

was at that time an almost insuperable difficulty in charging the alleged taxpayer except under Case V, inasmuch as the machinery specified by Section 106 of the Income Tax Act, 1842, could not be applied in respect of a trade wholly carried on in a place where there were no commissioners, and indeed in a country where the sovereignty was not the sovereignty of Great Britain. It was also pointed out that the terms of a section conferring certain exemptions or quasi-exemptions, namely, Section 39 of the Act of 1842, tended strongly to show that the case of a trade carried an wholly abroad was not taxable, except as a foreign possession. There were therefore those two elements: Case V was applicable, there was no machinery except under Case V, and further Section 39 tended strongly to show that Case I could not be applicable.

In the present case having regard to the fact that the company employing the appellant is a company situate in this country, having its registered office here, and that the source of income of the appellant is here, it is clear (for it has now been decided by the House of Lords) that Case V is not applicable, because the appellant is not in receipt of income arising from a possession out of the United Kingdom. *Foulsham* v. *Pickles* contains a number of illuminating judgments, not all perhaps taking precisely the same view of the law, or rather of the contruction of these difficult Acts. But when the matter went to the House of Lords it was held very distinctly that a man in the position of Mr. Pickles in that case and, I may say, in the same position as the appellant in this case, is not enjoying income arising from a possession out of the United Kingdom if the source of his income is in this country, and Lord Cave observed (94 L. J. K. B., at p. 421; [1925] A. C., at p. 465; 9 Tax Cas., at p. 288) that he was far from saying that Mr. Pickles could not have been assessed under Case II of Schedule D. Lord Buckmaster observed (94 L. J. K. B., at p. 422; [1925] A. C., at p. 467; 9 Tax Cas., at p. 290) that, Mr. Pickles being a person residing in the United Kingdom, it would appear that he was liable to be taxed under Schedule D, clause 1 (*a*) (ii), in respect of annual profits or gains arising from any trade, etc. But as pointed out he had been in fact assessed under Case V in paragraph 2.

Those observations are no doubt not any distinct guide to me in determining the position of the present appellant, but at any rate they do not tend in the opposite direction and the observations are a little difficult to explain, if it is reasonably clear, as is suggested on behalf of the appellant, that the Case of *Colquhoun* v. *Brooks*, which was in the minds of their Lordships and was referred to by them, shows beyond doubt that Case II does not apply to a case where the person employed renders his services wholly abroad.

To my mind there are two circumstances which have to be borne in mind in coming to the conclusion at which I have arrived. The proposition that there is a means of taxing the appellent under Case V is one which, for the reasons I have given, is inapplicable in this case. The proposition that it is impossible or very inconvenient to tax him owing to lack of machinery does not exist since the Income Tax Act, 1918, came into force, because by rule 4 of the miscellaneous rules applicable to Schedule D which form a part of that Act, there is provision under which he can be taxed where he ordinarily resides. The rule replaces Section 32 (1) of the Finance (No. 2) Act, 1915. The language of rule 4 of the miscellaneous rules is clearly and obviously different from that of Section 106 of the Act of 1842, and the Court is bound to pay attention to the fact that there is now no lack of machinery for taxing a man resident in this country who receives income in respect of services rendered wholly abroad, whether in a colony or in a foreign land.

Accordingly, as I think, both the grounds which caused the House of Lords to decide that Mr. Brooks was not liable under Case I of Schedule D fail to apply to the present case, and there is no reason for holding that Case II, which in terms covers the present case, is not an applicable Case under which the appellant may be charged as he has been charged. I would only add that for my part I am not convinced that he could not have been properly assessed and charged under Section 106 of the Income Tax Act, 1842, nor I am not satisfied that his employment within the meaning of that section was not to some extent exercised in part in Great Britain. We know that the source of his income was in Great Britain; we know that orders could be given to him in Great Britain, and I do not feel at all sure that to

some extent the employment within the meaning of that phrase in Section 106 was not exercised in Great Britain. However that may be, for the reasons I have given I agree with the decision of the learned Judge in the court below and I agree with my brethren in thinking that the appeal should be dismissed.

Appeal dismissed:
Leave to appeal to the House of Lords granted.

Solicitors:—*Dawson & Co.*, for the appellant. *Solicitor of Inland Revenue*, for the respondent.

NOTE.

[This decision of the Court of Appeal was affirmed by the House of Lords: See 20 Tax Cas. 566; 1937 A. C. 162—Ed.]

END OF VOL. IV.

PRINTED AT THE
COMPANY LAW INSTITUTE PRESS,
THYAGARAYANAGAR,
MADRAS.

INDIAN FINANCE ACT, 1936.

The following Act has been assented to by the Governor-General under the provisions of Clause (*b*) of sub-Section (1) of Section 67-B of the Government of India Act, and has been expressed to be made by the Governor-General under the provisions of sub-Section (2) of the same section, [*Vide* the Gazette of India, Part 4, dated the 4th April, 1936].

An Act to fix the duty on salt manufactured in, or imported by land into certain parts of British India, to fix maximum rates of postage under the Indian Post Office Act, 1898, and to fix rates of income tax and super tax.

Whereas it is expedient to fix the duty on salt manufactured in, or imported by land into, certain parts of British India, to fix maximum rates of postage under the Indian Post Office Act, 1898, and to fix rates of income tax and super tax; It is hereby enacted as follows:

1. Short title and extent.

(1) This Act may be called the Indian Finance Act, 1936.

(2) It extends to the whole of British India, including British Baluchistan and the Sonthal Parganas.

2. Fixation of salt duty.

The provisions of Section 7 of the Indian Salt Act, 1882, shall, in so far as they enable the Governor-General in Council to impose by rule made under that section a duty on salt manufactured in, or imported into, any part of British India other than Burma or Aden, be construed as if, for the year beginning on the 1st day of April, 1936, they imposed such duty at the rate of one rupee and four annas per maund or eighty-two and two-sevenths pounds avoirdupois of salt manufactured in, or imported by land into, any such part, and such duty shall, for all the purposes of the said Act, be deemed to have been imposed by rule made under that section.

3. Inland postage rates.

For the year beginning on the 1st day of April, 1936, the Schedule contained in the First Schedule to this Act shall be inserted in the Indian Post Office Act, 1898, as the First Schedule to that Act.

4. INCOME TAX AND SUPER TAX.

(1) Income tax for the year beginning on the 1st day of April, 1936, shall be charged at the rates specified in Part I of the Second Schedule, increased in each case by one-twelfth of the amount of the rate.

(2) The rates of super tax for the year beginning on the 1st day of April, 1936, shall, for the purposes of Section 55 of the Indian Income Tax Act, 1922, be those specified in Part II of the Second Schedule, increased in each case by one twelfth of the amount of the rate.

(3) For the purposes of the Second Schedule 'total income' means total income as determined for the purposes of income tax or super tax, as the case may be, in accordance with the provisions of the Indian Income Tax Act, 1922.

(4) For the purpose of any assessment to be made for the year ending 31st March, 1937, the rate of income tax applicable to such part of the total income of any person as is derived from salaries or from interest on securities paid in the year ending 31st March, 1936, shall be the previous year's rate, and for the purposes of refunds under sub-Section (1) or sub-Section (3) of Section 48 in respect of dividends declared in the year ending 31st March, 1936, or of payments made in the said year of salaries or of interest on securities, the rate applicable to the total income of the person claiming refund shall be the previous year's rate.

Explanation.—In this sub-section the term 'previous year's rate' with reference to any person means the rate of income tax which would have been applicable to his total income if he had been assessed for the year ending 31st March, 1936, on a total income equal to that on which he is assessable for the year ending 31st March, 1937.

SCHEDULE I.

Schedule to be inserted in the Indian Post Office Act, 1898.

[*See* Section 3.]

THE FIRST SCHEDULE

INLAND POSTAGE RATES.

[*See* Section 7.]

Letters.

For a weight not exceeding one tola ... One anna

For every tola, or fraction thereof, exceeding one tola ... Half an anna

Postcards

Single ...	Nine pies
Reply ...	One and a half annas

Book, Pattern and Sample Packets.

For the first five tolas or fraction thereof ...	Nine pies
For every additional five tolas or fraction thereof in excess of five tolas	Six pies

Registered Newspapers.

For a weight not exceeding ten tolas ...	Quarter of an anna
For a weight exceeding ten tolas and not exceeding twenty tolas ...	Half an anna
For every twenty tolas, or fraction thereof, exceeding twenty tolas ...	Half an anna

Parcels.

For a weight not exceeding twenty tolas ...	Two annas
For a weight exceeding twenty tolas and not exceeding forty tolas ...	Four annas
For every forty tolas, or fraction thereof, exceeding forty tolas ...	Four annas

SCHEDULE II

[*See* Section 4.]

PART I.

Rates of Income tax.

A. In the case of every individual, Hindu undivided family, unregistered firm and other association of individuals not being a registered firm or a Company.—

	Rate
(1) When the total income is Rs. 2,000 or upwards, but is less than Rs. 5,000 ...	Six pies in the rupee
(2) When the total income is Rs. 5,000 or upwards, but is less than Rs. 10,000 ...	Nine pies in the rupee

(3) When the total income is Rs. 10,000 or upwards, but is less than Rs. 15,000 ...	One anna in the Rupee
(4) When the income is Rs. 15,000 or upwards, but is less than Rs. 20,000 ...	One anna and four pies in the rupee
(5) When the total income is Rs. 20,000 or upwards, but is less than Rs. 30,000 ...	One anna and seven pies in the rupee
(6) When the total income is Rs. 30,000 or upwards, but is less than Rs. 40,000 ...	One anna and eleven pies in the rupee
(7) When the total income is Rs. 40,000 or upwards, but is less than Rs. 1,00,000 ...	Two annas and one pie in the rupee
(8) When the total income is Rs. 1,00,000 or upwards ...	Two annas and two pies in the rupee
B. In the case of every company and registered firm, whatever its total income ...	Two annas and two pies in the rupee

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PART II.

Rates of Super tax.

In respect of the excess over thirty thousand rupees of total income—

	Rate
(1) in the case of every company—	
(*a*) in respect of the first twenty thousand rupees of such excess ...	*Nil*
(*b*) for every rupee of the remainder of such excess ...	One anna in the rupee
(2) (*a*) in the case of every Hindu undivided family—	

(*i*) in respect of the first forty-five thousand rupees of such excess ...	*Nil*
(*ii*) for every rupee of the next twenty-five thousand rupees of such excess ...	One anna and three pies in the rupee
(*b*) in the case of every individual, unregistered firm and other association of individuals not being a registered firm or a company—	
(*i*) for every rupee of the first twenty thousand rupees of such excess ...	Nine pies in the rupee
(*ii*) for every rupee of the next fifty thousand rupees of such excess ...	One anna and three pies in the rupee
(*c*) in the case of every individual, Hindu undivided family, unregistered firm and other association of individuals not being a registered firm or a company—	
(*i*) for every rupee of the next fifty thousand rupees of such excess ...	One anna and nine pies in the rupee
(*ii*) for every rupee of the next fifty thousand rupees of such excess ...	Two annas and three pies in the rupee
(*iii*) for every rupee of the next fifty thousand rupees of such excess ...	Two annas and nine pies in the rupee
(*iv*) for every rupee of the next fifty thousand rupees of such excess ...	Three annas and three pies in the rupee

(*v*) for every rupee of the next fifty thousand rupees of such excess ...	Three annas and nine pies in the rupee
(*vi*) for every rupee of the next fifty thousand rupees of such excess ...	Four annas and three pies in the rupee
(*vii*) for every rupee of the next fifty thousand rupees of such excess ...	Four annas and nine pies in the rupee
(*viii*) for every rupee of the next fifty thousand rupees of such excess ...	Five annas and three pies in the rupee
(*ix*) for every rupee of the next fifty thousand rupees of such excess ...	Five annas and nine pies in the rupee
(*x*) for every rupee of the remainder of such excess ...	Six annas and three pies in the rupee

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